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ABSTRACT

This January 1996 audit report reviews the management of the Economic Development Program by the Chancellor's Office of the California Community Colleges and reviews the funding procedures of the Chancellor's Office and the Department of Education relating to the State Plan for Vocational Education. The state auditor found that the Chancellor's Office did not comply with procedures for awarding grants and did not adequately oversee the colleges' compliance with grant requirements. In 1992-93, there was no evidence of a competitive basis to award 33 of 55 grants reviewed, despite procedures calling for competitive awards. The Office did not ensure that community colleges submitted required financial reports, and the colleges did not always spend funds in accordance with grant requirements. Additionally, the Chancellor's Office and the Department of Education circumvented state controls by using fiscal agents to obtain contractor services and submitted erroneous and misleading information to the Department of General services as support for contract approval requests. This audit recommends that the Chancellor's Office comply with the policy of competitive grant processes, monitor and review grant expenditures at the colleges, discontinue use of fiscal agents, and ensure contracts have been approved and amounts paid to contractors is appropriate. The audit also recommends that the Chancellor's Office reimburse the state for the amount of unnecessary costs incurred as a result of inadequate management. (RDG)

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California Community Colleges:

The Chancellor's Office Inadequately Controlled Its Economic Development Program and, Along With the Department of Education, Circumvented State Contracting Procedures

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CALIFORNIA STATE AUDITOR

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January 4, 1996 94123

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As requested by the Joint Legislative Audit Committee, the Bureau of State Audits presents its audit report concerning the Chancellor's Office's administration of the Economic Development Program. In addition, the report addresses the Chancellor's Office and the Department of Education's (department) process for preparing the Needs Assessment and State Plan for Vocational Education. This report concludes that the Chancellor's Office lacks adequate control over the Economic Development Program. Specifically, the Chancellor's Office did not comply with its own procedures for awarding Economic Development Program grants, and did not ensure that community colleges complied with grant requirements.

The report also concludes that the Chancellor's Office and the department inappropriately circumvented state controls by using fiscal agents to obtain the services of a specific contractor. In addition, the Chancellor's Office and the department submitted erroneous and misleading information to the Department of General Services as support for their requests for approval of contracts and amendments. Finally, by using fiscal agents to pay the contractor, neither the Chancellor's Office nor the department can assure that the amounts paid to the contractor were appropriate or reasonable.

Respectfully submitted,

Kurt R. Sjoberg

KURT R. SJOBERG
State Auditor

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Table of Contents

Summary	***S-1***
Introduction	***1***
Chapter 1	
The Chancellor's Office Lacks Adequate Control Over the Economic Development Program	5
Recommendations	***24***
Chapter 2	
The Chancellor's Office and the Department of Education Used Fiscal Agents To Circumvent State Controls To Develop the State Plan	25
Recommendations	***40***
Appendix A	
Description of Economic Development Program Initiatives Funded by the Chancellor's Office	43
Appendix B	
Chronology of Key Events in Preparation of the Vocational Education Needs Assessment and State Plan	49
Responses to the Audit	
Chancellor's Office of the California Community Colleges	53
California State Auditor's Comments on the Response by the Chancellor's Office of the California Community Colleges	***77***

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Department of Education 83

California State Auditor's Comments on the Response by the Department of Education 89

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Summary

Audit Highlights ...

The Chancellor's Office:

- ☑ ***Did not always use a competitive process to award grants to community colleges.***
- ☑ ***Does not adequately monitor and review grant expenditures.***
- ☑ ***Incurred unnecessary costs of $15,500 by paying its deputy chancellor through an interjurisdictional contract.***
- ☑ ***Did not ensure that community colleges complied with all grant requirements.***

The Chancellor's Office and the Department of Education:

- ☑ ***Circumvented state controls by using fiscal agents.***
- ☑ ***Submitted erroneous and misleading information to the Department of General Services.***

The Board of Governors of the California Community Colleges (board) was established to provide statewide leadership to California's community colleges. The Legislature appropriates funds to the board for the support of the Chancellor's Office and for various local assistance programs administered by the community college districts, such as the Economic Development Program. The mission of the Economic Development Program is to advance California's economic growth and competitiveness through quality education and services. To accomplish this mission, the Chancellor's Office awards grants to various community colleges throughout the State to support the community colleges' efforts to provide education, training, and technical services to California business and industry. Our review focused on the Chancellor's Office's procedures for awarding Economic Development grants and monitoring and reviewing grant expenditures. Specifically, we noted the following concerns:

- The Chancellor's Office's annual Economic Development Program Funding Plans state that it uses a competitive process to award grants to community colleges. However, for 33 of the 53 grants we reviewed for fiscal years 1992-93 and 1993-94, the Chancellor's Office could not provide evidence that it used a competitive basis to award the grants.

- The Chancellor's Office did not adequately monitor and review grant expenditures to ensure that community colleges were complying with grant requirements. Specifically, the Chancellor's Office did not ensure that community colleges submitted required financial reports and did not adequately review the reports that it did receive.

- Community colleges did not always spend funds in accordance with the approved budget. For example, Chaffey College used a portion of its fiscal year 1993-94 grant to purchase computer equipment costing $41,000. However, the approved grant did not authorize any funds for the purchase of equipment.

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- Community colleges did not always comply with other grant requirements. For example, four of the five community colleges we tested did not provide adequate matching funds for at least one of the grants they received.

- The State Center Community College (State Center) may have incurred excessive travel costs. For example, State Center exceeded its per diem rate for meals in at least 51 instances. As a result, State Center paid approximately $10,000 more for meals than per diem rates allow.

- The Chancellor's Office inappropriately used Chaffey College as a fiscal agent to pay contractors who were working at State Center.

- The Chancellor's Office inappropriately used an interjurisdictional exchange contract, thereby incurring additional costs to the State of approximately $15,500. Specifically, the Chancellor's Office continued to pay its deputy chancellor through an interjurisdictional exchange contract with State Center from July 1991 through June 1994, even though he had been appointed to an exempt position in July of 1991.

We were also asked to determine whether the Chancellor's Office used federal funds for the program in accordance with the Vocational Education State Plan (state plan). The state plan addresses Vocational Education programs rather than Economic Development programs; however, because our initial review of contracts that the Chancellor's Office and the Department of Education (department) issued to obtain assistance in preparing the state plan raised concerns, we expanded the scope of our audit. Specifically, we examined the process that the Chancellor's Office and the department used to obtain the services of community colleges and a private contractor to prepare the state plan for 1994-96. During this review, we noted the following concerns:

- The Chancellor's Office and the department circumvented state controls by using fiscal agents to obtain the services of The Resource Group (contractor) to prepare both the Vocational Education needs assessment and state plan. The Chancellor's Office and the department paid these fiscal agents approximately $62,000 in administrative

tees. Furthermore, the $1.2 million paid to the contractor exceeded the budget for the needs assessment and the state plan by approximately $120,000.

- The Chancellor's Office and the department submitted erroneous and misleading information to the Department of General Services as support for its requests for approval of contracts and amendments.

- The Chancellor's Office allowed the contractor to begin work prior to approval of its sole-source contract and the department allowed the contractor to perform services without having any formal agreement with either the department or its fiscal agent.

- Employees at two of the entities that the Chancellor's Office and the department used as fiscal agents, Chaffey College and East San Gabriel Valley Regional Occupational Program, had recently been employed by the contractor. Therefore, by using them as fiscal agents, the Chancellor's Office and the department may have caused them to violate the common law doctrine against conflicts of interest.

- By using fiscal agents, the Chancellor's Office and the department lacked control over payments made for the needs assessment and the state plan. Therefore, the two agencies cannot ensure that the amounts paid to the contractor were appropriate or reasonable.

The board has adopted new policies regarding approval and use of grants and contracts at the Chancellor's Office. Specifically, in September 1995, the board adopted a policy stating that contracts must be reviewed by it if amended in such a way as to make them exceed either $100,000 or three years in duration, or if they involve consulting services over $50,000.

The board also adopted a policy that requires the Chancellor's Office to seek board approval before entering into any grants which exceed $100,000 or three years in duration. Although the revised policy improves control over the process for awarding grants, it includes a provision that states that the new procedures shall not apply to grants distributed on an allocation formula basis that has been reviewed and approved by the board. Since many of the grants awarded by the Chancellor's Office are distributed

based on an allocation formula basis, including grants for the Economic Development Program, those grants would be exempt from the revised board policies. Therefore, the board should reconsider the provision in its policy that excludes these grants.

In addition, the Chancellor's Office has created a Grants and Contracts processing unit as part of the Fiscal Division. This unit processes grant awards, verifies and logs quarterly and final fiscal reports, and reconciles fiscal data with the accounting unit. Specialists in the Economic Development and Vocational Education Division monitor the programmatic aspects of the grants. Finally, the Grants and Contracts unit maintains the master files for audit purposes.

The Superintendent of Public Instruction of the Department of Education has implemented new policies regarding approval and use of contracts at the department. Specifically, in January 1995, the superintendent issued a policy stating that effective immediately she will review all proposed contracts. In addition, she stated that requests to extend contracts beyond the original ending date must be accompanied by a full explanation of the reason for the extension and a summary of the work completed to date. The superintendent also stated that effective April 1, 1995, contracts not fully executed by the starting date will receive personal review by her as to the reasons for the delay. Furthermore, the superintendent discouraged the use of sole-source contracts, stating that any requests for such contracts will be closely reviewed and approved by her. Finally, she stated that it will no longer be acceptable to circumvent appropriate contracting procedures through Budget Act language that mandates a specific contractor.

Recommendations

To ensure adequate control over Economic Development Program funds, the Chancellor's Office should:

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- Comply with its policy of using a competitive process to award Economic Development grants;
- Monitor and review grant expenditures to ensure that community colleges are complying with grant requirements; and

- Require community colleges to comply with the State's per diem policy for travel expenses.

The Chancellor's Office should also reimburse the State for the amount of unnecessary costs incurred as a result of its inappropriate use of an interjurisdictional exchange contract.

The Chancellor's Office and the department should:

- Discontinue the use of fiscal agents to circumvent state controls;

- Comply with state requirements for awarding contracts and submit complete and accurate information to the Department of General Services when requesting approval of contracts;

- Ensure that the Department of General Services has approved its contracts before allowing contractors to commence work; and

- Determine whether the amounts paid to the contractor for the needs assessment and the state plan were appropriate and, if necessary, recover any overpayments.

Agency Comments

The Chancellor's Office agrees with many of the findings in the report and it plans to give serious consideration to our recommendations. However, the Chancellor's Office disagrees with our conclusion that by paying the deputy chancellor through a contract with State Center it circumvented the state budget process and it created a conflict of interest by allowing the deputy chancellor to approve grants to State Center. In addition, the Chancellor's Office did not agree that State Center incurred excessive travel costs. Finally, with respect to payments for the state plan, the Chancellor's Office disagrees with our conclusion that it can neither assure that it received the services it paid for, nor that the costs paid for the services were reasonable.

The department generally supports the recommendations for ensuring compliance with state contracting requirements. However, the department disagrees with our final recommendation suggesting that it determine whether amounts paid to the contractor were appropriate.

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Introduction

The Board of Governors of the California Community Colleges (board) was established to provide statewide direction, coordination, and leadership to the public community college segment of California higher education. The board seeks to ensure the most prudent use of public funds and to improve district and campus programs through informational and technical services. The Legislature appropriates funds to the board for the support of the Chancellor's Office and for various local assistance programs administered by the community college districts, such as the Economic Development Program. During fiscal year 1994-95, the Economic Development Program received approximately $6,973,000 in state funds.

In 1988, the Chancellor's Office established the Economic Development Program to support local community colleges' efforts to provide education, training, and technical services to California business and industry. In 1991, the Legislature codified the mission of the program by amending the California Government Code, Section 15739.32, to include the Economic Development Program. The mission of the Economic Development Program, in part, is to advance California's economic growth and global competitiveness through quality education and services focusing on continuous workforce improvement, technology deployment, and business development.

To accomplish the mission of the Economic Development Program, the Chancellor's Office established a series of continuing and annual program initiatives such as Centers for Applied Competitive Technologies, Statewide Coordination Network, and Workplace Learning Resource Centers. Each year the Chancellor's Office distributes information to the community colleges describing the initiatives and the amount of available funding. Appendix A provides a description for each of the program initiatives funded by the Chancellor's Office during fiscal years 1992-93 and 1993-94, the period of our review.

In its 1995-96 expenditure plan for the Economic Development Program, the Chancellor's Office stated that it initially awards grants for continuing initiatives based on responses to Requests for Qualifications (RFQ). The RFQ has prescriptive criteria, a specific scope of work, and requires a site visit as part of the review process. However, after the Chancellor's Office awards the initial grant, community colleges receive continuous funding for the initiative based on their performance and the availability of funds. The Chancellor's Office also states that it uses a Request for Application (RFA) process to award funds for annual initiatives.

The Chancellor's Office develops the requests through the collaborative efforts of government agencies and representatives of business, industry, and labor. Community colleges must submit responses to RFQs or RFAs to be eligible to receive initial funding for any of the initiatives. The Chancellor's Office uses teams from state and local agencies and private sector businesses to review and evaluate the responses. The review teams recommend funding for responses that meet or exceed specific criteria and that receive the highest ratings.

Scope and Methodology

The purpose of this audit was to evaluate the Chancellor's Office's administration of the Economic Development Program (program). Specifically, we reviewed the process that the Chancellor's Office used to award grants and contracts to the community colleges to determine if it complied with applicable laws and regulations and its own policies for awarding grants for the various initiatives in the program. In addition, we evaluated any controls that the Chancellor's Office had established to distribute the funds and whether those controls are consistent with state and federal laws and regulations. Finally, we evaluated hiring and employment practices used by the Chancellor's Office for staff employed to administer the program to determine compliance with applicable laws and regulations.

To determine the process that the Chancellor's Office used to award grants for the various program initiatives, we interviewed staff in the Economic Development Division and at the community colleges at which we conducted site visits. In addition, we reviewed expenditure plans that described the process that the Chancellor's Office used to solicit proposals from the various community colleges and to review and evaluate those proposals.

To determine how the Chancellor's Office controls program funds, we reviewed the policies and procedures used to distribute the funds. We interviewed staff at the Chancellor's Office and various community colleges to gain an understanding of the procedures used to track and report expenditures and to monitor grantees. We also reviewed quarterly and yearly expenditure and progress reports that the community colleges submitted to the Chancellor's Office. Finally, we visited five community college districts and reviewed invoices, timesheets, and other documentation supporting the expenditures for the grants that the Chancellor's Office had awarded to the respective districts.

To examine whether the Chancellor's Office followed appropriate hiring and employment practices for staff employed to administer the program, we determined whether personnel assigned to the program were state or contract employees. In addition, we reviewed the activities of all employees whose salaries and expenses were being paid with program funds to ensure that the work these employees performed was directly related to the respective program initiatives.

Finally, we reviewed an Interjurisdictional Exchange contract that the Chancellor's Office entered into with State Center Community College to determine whether the Chancellor's Office complied with state laws, rules, and regulations regarding the use of such agreements. To determine whether the payments that the Chancellor's Office made for the contract were appropriate, we reviewed the documentation supporting the payments.

We were also asked to determine whether the Chancellor's Office used federal funds for the program in accordance with the Vocational Education State Plan (state plan). The state plan addresses Vocational Education programs rather than Economic Development programs; however, because our initial review of contracts that the Chancellor's Office and the Department of Education issued to obtain assistance in preparing the state plan raised concerns, we expanded the scope of our audit. Specifically, we examined the process that the Chancellor's Office and the Department of Education used to obtain the services of community colleges and private contractors to complete the state plan for 1994-96 to determine compliance with applicable laws and regulations. We also interviewed staff at the community colleges and a regional occupation program to determine how these local agencies were selected and how they selected subcontractors.

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Chapter 1

The Chancellor's Office Lacks Adequate Control Over the Economic Development Program

Chapter Summary

The Chancellor's Office lacks adequate control over Economic Development Program funds. Specifically, we found that the Chancellor's Office did not always comply with its own procedures for awarding Economic Development grants. Additionally, it does not adequately monitor the community colleges to ensure that they are complying with grant requirements. For example, the community colleges did not always spend funds in accordance with the approved grant budget. The expenditures recorded in some community colleges accounting records did not always agree with the expenditures reported to the Chancellor's Office. Some community colleges did not provide adequate matching funds, as required by the grant agreements, and some did not obtain approval from the Chancellor's Office prior to awarding subcontracts. Also, the community colleges did not use a competitive process to award their subcontracts.

We noted that the Economic Development grants allowed the community colleges to reimburse travel costs at district rates, which in some cases were well in excess of the State's rates. In addition, State Center Community College District (State Center) incurred excessive travel costs.

The Chancellor's Office may not be maximizing Economic Development funds. Instead of recovering unspent funds by withholding them from future apportionments, it has extended the time frame for completion of project activities. This denies other community colleges the opportunity to receive grants from this unspent money.

The Chancellor's Office also circumvented the state budget process and incurred additional costs by paying the salary of its deputy chancellor through a contract with State Center. Specifically, the Chancellor's Office reimbursed State Center for the deputy chancellor's salary from June 1990 through June 1994 even though the Chancellor had appointed him to an exempt state position in July 1991. In addition, because the deputy chancellor was an employee of State Center before his

appointment, the Chancellor's Office created a conflict of interest when it allowed him to approve grants that it awarded to State Center.

The Chancellor's Office Does Not Adhere to Its Own Procedures

The Economic Development Program consists of a series of continuing and annual program initiatives established to advance economic development in the State of California. According to its Economic Development Funding Plans (funding plan), the Chancellor's Office uses a competitive bidding process to award grants for continuing initiatives in the first year. Once funded, the grants are continued without competitive bid, based on performance and the availability of funding. In contrast, the Chancellor's Office uses a competitive bid process to award grants for its annual initiatives. The actual number of grants funded for annual initiatives depends on the availability of funds and the number of applications received.

During fiscal years 1992-93 and 1993-94, the period of our review, the annual funding plan, which must be approved by the California Community Colleges Board of Governors, stated that to be eligible for funding colleges must submit a response to a Request for Qualifications (RFQ) for continuing programs. In addition, for annual programs, colleges had to submit either a response to a Request for Proposal (RFP) or an Application for Funding. Review teams rank the RFQs and RFPs according to criteria common to all funding requests. The Chancellor's Office awards grants, contingent upon the availability of funding, to the community colleges who receive the highest rank. Applications for Funding are reviewed by Chancellor's Office staff who negotiate new program activities and objectives on an annual basis and recommend the program to the chancellor for funding.

Chancellor's Office did not always use a competitive process to award grants.

We found that the Chancellor's Office did not always comply with its own procedures when awarding grants for the Economic Development Program. Specifically, the Chancellor's Office could not provide evidence that it used a competitive process to award 8 of the 28 grants we tested. Four of the 8 grants were for the initial year the community colleges received the continuing program grant, and 4 grants were for annual programs. Thirteen of the remaining 20 grants were for continuing initiatives for which the Chancellor's Office had awarded the funds in a prior fiscal year; therefore, the bid and review process did not apply. The other 7 grants, for annual initiatives, were competitively bid.

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Because only 15 of the 28 grants we selected required the Chancellor's Office to use a competitive process to award the grants, we selected an additional sample of 25 grants for programs that started in either fiscal year 1992-93 or 1993-94. Although all of these grants should have been awarded using a competitive process, the Chancellor's Office could not provide evidence that it used a competitive process to award any of these grants.

For example, Los Rios Community College District (Los Rios) received a grant, totaling approximately $96,000, for fiscal year 1992-93 to act as the northern coordinator for the Regional Economic Development and Contract Education Technical Support initiative. Although this is a continuing initiative, fiscal year 1992-93 was the first year that it was awarded to Los Rios; therefore, the award should have been based on a competitive bid. However, neither Los Rios nor the Chancellor's Office could provide evidence of a competitive bid process. The Chancellor's Office sent a letter to Los Rios in May 1992, prior to awarding the grant, requesting it to submit an annual program plan that "would serve in lieu of a proposal." According to the specialist of the Economic Development Program, annual program plans are requested only after the first year of a continuing initiative, and proposals must be submitted by colleges to initially receive a grant for continuing initiatives. Since fiscal year 1992-93 was the first year the grant was awarded to Los Rios, the Chancellor's Office should have requested a proposal rather than an annual program plan.

All community colleges may not have a fair chance to compete for Economic Development funds.

The Chancellor's Office sent similar letters in May 1992 to Rio Hondo College to act as the southern coordinator for the Regional Economic Development and Contract Education Technical Support initiative, and to Fullerton College for the Statewide Workplace Learning Resource Leadership and Technical Assistance initiative. Since these are continuing initiatives and neither college had received the grant prior to fiscal year 1992-93, the Chancellor's Office should have used a competitive process to award the grants. By not awarding the Economic Development Program funds using a competitive bidding process, the Chancellor's Office has no assurance that the most qualified colleges receive the monies. Additionally, by subjectively selecting the recipient college, the Chancellor's Office cannot ensure that all community colleges have a fair and equitable chance to receive Economic Development funds.

During our review we also noted that the Chancellor's Office did not follow its own guidelines for mailing RFPs and RFQs to the community colleges. Delays in mailing the RFPs or RFQs may cause subsequent delays in awarding the grants to the community colleges. According to its funding plan for fiscal

year 1992-93, the Chancellor's Office intended to mail the RFPs and RFQs to the community colleges by January 31, 1992. We reviewed four annual initiatives for which the Chancellor's Office had the bid and review documents on file, and in all four cases the Chancellor's Office had not mailed the RFPs until March 6, 1992. For five of the six continuing initiatives that we tested for fiscal year 1992-93, the Chancellor's Office did not send letters to the colleges requesting the annual program plan until May 23, 1992.

Late mailings of RFPs and RFQs caused delayed grant awards.

The fiscal year 1993-94 funding plan stated that RFPs and RFQs would be mailed by February 5, 1993. However, the Chancellor's Office did not mail the RFPs for both of the annual initiatives to be reviewed until at least March 26, 1993. The Chancellor's Office did not mail letters requesting the annual program plans for the six continuing initiatives we reviewed until May 5, 1993. These letters required the community colleges to submit their annual program plans by May 25, 1993.

Because the Chancellor's Office did not mail the RFPs and RFQs in a timely manner, it was not able to review the proposals and award the grants prior to the start date. As a result, some community colleges began work before the Chancellor's Office approved their grant. The community colleges began work before the Chancellor's Office approved their grant for 12 of the 28 grants that we reviewed. For example, State Center received a grant totaling approximately $600,000 for fiscal year 1992-93. While State Center started work on July 1, 1992, the Chancellor's Office did not approve the grant until November 2, 1992. Similarly, in 1993, State Center began work on its Locally-Based Statewide Coordination Network grant on July 1, 1993, even though the Chancellor's Office did not approve the grant until September 15, 1993.

The Chancellor's Office Does Not Adequately Monitor Grant Expenditures

The Chancellor's Office does not adequately monitor and review Economic Development expenditures incurred by grant recipients. Specifically, the Chancellor's Office does not ensure that community colleges submit the required financial reports or that submitted reports are adequately reviewed. The Chancellor's Office also does not review supporting documentation for expenditures or subcontracts entered into by the community colleges. Because it lacks adequate controls over grant expenditures, the Chancellor's Office has no assurance that community colleges are spending funds in accordance with grant requirements. Because it does not

adequately oversee its grantees, the Chancellor's Office cannot ensure that the amounts reported in the fiscal reports submitted by community colleges are accurate.

The Community Colleges Did Not Provide Sufficient Matching Funds

The terms and conditions of the Economic Development grants require community colleges to provide matching funds equal to the amount of Economic Development funds they receive. The grants do not allow the community colleges to count Economic Development funds received from other community colleges as matching funds. Because they do not require supporting documentation for matching funds claimed by the community colleges, the Chancellor's Office cannot ensure the community colleges are providing sufficient matching funds, as required.

Four of the five community colleges reviewed failed to provide from $32,000 to $327,000 in matching funds.

As Table 1 shows, four of the five community colleges we tested did not provide a sufficient amount of matching funds. For example, Chaffey College received a grant totaling $121,000 in fiscal year 1992-93. Although the terms and conditions of the grant required Chaffey College to provide funds in an amount equal to the grant funds, it did not provide any matching funds.

Table 1

Grant Dollars Not Matched (Rounded to Thousands)

College	Number of Grants Reviewed	Number of Grants Not Sufficiently Matched	Total Amount of Grant Funds Spent	Amount of Grant Funds Not Matched
Chaffey	2	2	$ 327,000	$327,000
El Camino	2	0	1,600,000	0
Los Rios	3	2	246,000	32,000
Rio Hondo	2	1	125,000	67,000
State Center	2	1	600,000	39,000

Furthermore, the community colleges inappropriately reported some amounts as matching funds. In fiscal year 1992-93, State Center received a grant totaling $599,830 and reported matching funds of $740,000; however, we question the method it used to determine the amount of in-kind matching funds. State Center claimed $3,000 for each individual who attended a series of one-day California Supplier Improvement Program meetings as matching funds. State Center calculated the $3,000

by assuming that each person who attended the meetings had an annual salary of $100,000 and that each meeting represented approximately 3 percent of the individual's annual workload.

We believe that State Center's methodology resulted in inflated totals. For example, based on a work year of 1,920 hours (160 hours per month), 3 percent of an individual's time represents approximately 58 hours. Therefore, State Center's claim that each one-day meeting represents 3 percent of the attendee's time is grossly overstated. Some individuals were listed as having attended multiple meetings. For example, one individual was listed as having attended six different meetings. Using State Center's rate of 3 percent per meeting, this person spent 18 percent of his annual workload donating time to State Center. Using the estimate of 1,920 working hours in a year, 18 percent of this individual's time equals 346 hours, or 43 days. Based on the documentation provided to us by State Center, this individual attended six one-day meetings. Because we feel that State Center's methodology for calculating in-kind matching funds is seriously flawed, we believe that State Center inappropriately included $105,000 in its matching funds for fiscal year 1992-93.

State Center's methodology for calculating in-kind matching funds is seriously flawed, and Rio Hondo College overstated its matching funds by $67,000.

State Center also included in its fiscal year 1992-93 matching fund calculation $13,900 from Chaffey College and $51,500 from Rio Hondo College. These amounts were paid from Economic Development grants at those colleges; therefore, State Center inappropriately used $65,400 of Economic Development funds from grants the Chancellor's Office awarded to other community colleges as matching funds for its grant.

Additionally, we determined that Rio Hondo College overstated the amount of matching funds for one of its Contract Education Technical Support grants by $67,000. In fiscal year 1993-94, Rio Hondo College included in-kind matching funds for conferences conducted by the grant's project director. Specifically, Rio Hondo College included $50 per hour for each person who attended the conferences. However, Rio Hondo College could not demonstrate how by merely attending these seminars the individuals contributed toward the grant objectives. Rio Hondo College also included as matching funds $50 per hour for certain telephone calls made by the project director. Speaking at conferences and conferring with private businesses and community colleges about the Economic Development program are part of the required duties of the project director.

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The RFPs and RFQs state that actual auditable resources dedicated to the projects will be considered as a match. These may take the form of dollars, equipment, facilities, and personnel time. We believe that the community colleges should include only those services that can be identified as having directly contributed toward the fulfillment of the grant requirements. By not requiring the community colleges to provide the required amount of matching funds, the Chancellor's Office is not ensuring that the community colleges are maximizing the effectiveness of the Economic Development Program and, thus, maximizing the use of state resources. Furthermore, by not contributing the required amount of matching funds, the community colleges are not providing additional resources that could benefit the program.

The Chancellor's Office Does Not Ensure That Community Colleges Submit Required Reports

The terms and conditions of the Economic Development grants require the community colleges to submit quarterly progress and fiscal reports to the Chancellor's Office. They must also submit both a final fiscal and a final narrative report within 30 days of completing the project. Finally, the grants require the community colleges to submit progress reports every 90 days for performance extended beyond June 30. Our review revealed that the Chancellor's Office does not ensure that the community colleges submit all required reports and does not adequately review the reports that it does receive.

Chancellor's Office could not provide evidence of receiving all progress and fiscal reports.

We attempted to obtain and review the required reports for 28 grants awarded in fiscal years 1992-93 and 1993-94. The Chancellor's Office could not provide us all four quarterly progress reports for 16 of 28 grants. It also could not provide evidence that it had received all four quarterly fiscal reports for 17 of the 28 grants. According to the Economic Development Program specialist, the Chancellor's Office received all required reports; however, it did not file them appropriately due to lack of available staff. As a result, it could not locate many of the reports.

In addition to the reviews we conducted at the Chancellor's Office, we also attempted to review the progress and fiscal reports during our site visits to five community colleges. However, contrary to the Chancellor's Office assertion that it had received all of the required reports, we determined that three of the five colleges did not submit all of them. For example, Chaffey Community College submitted only 5 of 18

required reports for the two grants we reviewed. Additionally, Rio Hondo submitted only 15 of 28 required reports for the four grants it received in fiscal years 1992-93 and 1993-94.

The Community Colleges Do Not Comply With All Grant Requirements

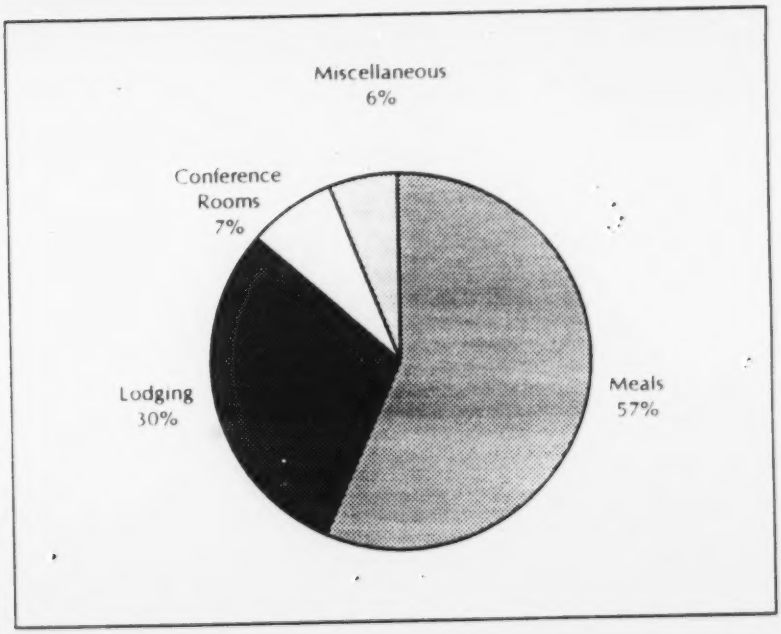
The Economic Development grant agreements establish certain requirements that the community colleges must adhere to when spending the grant funds. For example, the grant agreements require the community colleges to limit travel expenditures to those necessary for the performance of the grant. Community colleges are also required to obtain written approval from the Chancellor's Office before entering into subcontracts and provide evidence that cost was considered when awarding subcontracts. Finally, community colleges must adhere to the approved budget when spending grant funds. We found that the community colleges do not always comply with these grant requirements.

State Center Community College District Travel Costs Appear Excessive

The terms and conditions of the Economic Development grants allow community colleges to reimburse staff for travel expenditures in accordance with policies adopted by the respective college's governing board. However, they also require the community colleges to limit travel expenditures to those necessary for the performance of the grant. Our review of travel expenditures charged to the Economic Development Program showed that State Center may be incurring excessive travel and related costs. We reviewed a sample of 44 invoices totaling approximately $67,000 for conferences and staff meetings held at various hotels. The travel costs included approximately $38,000 for meals, $20,000 for lodging, $5,000 for conference room fees, and $4,000 for miscellaneous items, such as equipment rentals and photocopies.

Figure 1

Travel Expenditures for Staff Meetings and Conferences by Category



Source: Percentages based on 44 invoices reviewed at State Center Community College.

As shown in Figure 1, State Center spent 57 percent of these conference and staff meeting expenditures for meals. While we agree that periodic conferences and staff meetings are important, we found that some of the costs for the meals at these conferences appear excessive and exceed amounts established in State Center's own travel policy. Although conferences differ from individual travel, the district should prudently spend state grant funds. The policy provides that travel expenditures will be reimbursed in accordance with the State's per diem policy. For example, the State's reimbursement rate for lunch is the lesser of actual cost or $9.50. However, State Center paid $731 for a lunch for 27 people who attended a conference at the Westin Hotel, a cost of $27 per person. In another instance, State Center paid $848 for a luncheon attended by 31 people, a cost of approximately $27 per person, at a conference conducted at the Hyatt Islandia in San Diego. The State's reimbursement rate for dinner is the lesser of actual cost or $17, but at the same conference State Center paid $1,231 for a dinner attended by 45 people, again at a cost of approximately $27 per person.

24

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Of the 258 travel invoices we reviewed, which included conferences, for fiscal years 1992-93 and 1993-94, State Center paid for meals in excess of state per diem rates in 51 instances (20 percent). As a result, State Center paid approximately $10,000 more for meals than it would have had it complied with its travel policy.

Furthermore, we noted five instances totaling approximately $1,700 where State Center inappropriately paid for lodging expenditures. For example, State Center paid travel costs totaling $914 for both the deputy chancellor and vice chancellor from the Chancellor's Office. These costs should have been paid by the Chancellor's Office.

Grant funds would be maximized if community colleges were required to follow state travel rates.

Although State Center's per diem policy requires the district to comply with the State's regulations for reimbursing travel costs, the reimbursement rates at the remaining four community colleges exceed the state rates. The grant agreements we reviewed require the community colleges to comply with district travel rates rather than state per diem rates. Because the program is funded with state resources, we believe the Chancellor's Office should modify its grant agreements to require the community colleges to comply with the State's per diem policy for all travel-related expenditures. This would provide added assurance that grant funds are used effectively and that the cost of travel funded with state resources is reasonable.

The Community Colleges Do Not Follow Subcontracting Requirements

The Economic Development grants require community colleges to obtain written approval from the Chancellor's Office before entering into subcontracts, except when those subcontracts are specifically identified in the grants. In addition, the grants require the community colleges to select subcontractors using procedures that will ensure that cost is given substantial weight and that the selected subcontractor is the best qualified party available. One method that the community colleges could use to ensure both of these requirements are met is to solicit bids from multiple vendors.

As Table 2 indicates, four of the community colleges we tested failed to obtain written approval from the Chancellor's Office before entering into subcontracts. For example, State Center entered into six subcontracts in fiscal year 1992-93 and six subcontracts in fiscal year 1993-94; however, they did not obtain written approval in any of these instances.

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In addition, the four community colleges failed to use the proper selection process, which includes obtaining competitive bids when entering into subcontracts. Chaffey College, for example, entered into a total of 10 subcontracts in fiscal years 1992-93 and 1993-94 and in each instance awarded sole-source subcontracts to vendors rather than solicit competitive bids.

Table 2

Grants for Which Community Colleges Did Not Obtain Prior Approval and Did Not Use Competitive Process To Hire Subcontractors

Community College	Fiscal Year	Number of Grants Reviewed	Total Amount of Grants	Amount Paid to Subcontractors Reviewed	Number of Subcontractors Reviewed	Hired Without Prior Approval	Number for Which Colleges Did Not Use Competitive Bids
Chaffey	1992-93	1	$121,086	$103,000	5	5	5
	1993-94	1	206,084	108,600	5	5	5
El Camino	1992-93	1	811,000	78,048	1	1	1
	1993-94	1	811,000	130,000	6	6	6
Los Rios	1992-93	1	245,940	78,601	2	1	2
State Center	1992-93	1	599,830	253,122	6	6	6
	1993-94	1	499,830	198,469	6	6	6

Furthermore, State Center failed to obtain written agreements with four of its subcontractors during fiscal years 1992-93 and 1993-94 and paid them $49,977 and $131,014, respectively.

By not obtaining the required approvals from the Chancellor's Office for subcontracts and by not using procedures to ensure that cost is given substantial weight in the selection process, the community colleges cannot ensure that the costs incurred were reasonable and competitive nor that the most qualified vendor was selected. Additionally, by not ensuring all contracts are written agreements, State Center created a risk that public funds would be gifted should the contractor fail to complete the activities for which it was being paid.

The Community Colleges Do Not Always Stay Within the Approved Grant Budget

All five community colleges we reviewed exceeded budget category limits without approval from the Chancellor's Office.

The Economic Development grants state that the Chancellor's Office will pay costs as specified in the budget and expenditure plan. The grant agreements also state that changes in individual budget categories, such as salaries or equipment, cannot be made without either prior written approval from the Chancellor's Office or a formal grant amendment, depending on the amount of the change. Our review of 14 grants at five community colleges found that, while overall budgets were not exceeded, all five colleges exceeded the approved budget in one or more categories for 10 of the 14 grants. As shown in Table 3, the community colleges exceeded their budget authority by as much as 263 percent for certain expenditure categories.

Table 3

Amount and Percentage Actual Expenditures Exceeded Budgeted Amounts

College Awarded Each Grant	Number of Categories That Exceeded Budget	Total Budget for Categories	Amount Budget Exceeded	Percent by Which Categories Exceeded Budget
Chaffey	2	$ 4,843	$ 12,774	263%
Chaffey	5	0	59,794	*
El Camino	1	656,477	34,680	5
El Camino	4	411,000	124,998	30
Los Rios	1	79,750	9,990	12
Rio Hondo	2	63,737	3,347	5
Rio Hondo	3	49,605	2,685	5
Rio Hondo	1	0	1,880	*
State Center	5	318,010	30,228	9
State Center	6	152,271	15,492	10

* Colleges spent funds for which no amounts were budgeted.

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None of the community colleges we tested obtained written approval from the Chancellor's Office to exceed their budget for a particular category. For example, Chaffey College used $41,000 of funds from a grant it received in fiscal year 1993-94 to purchase computer equipment for State Center. However, the approved budget for the grant did not authorize any funds for the purchase of equipment. Similarly, in fiscal year 1992-93, State Center received a grant totaling $599,830 that included a budget of $268,680 for consultants, but it actually

spent $284,068 in this category; however, it did not obtain prior approval from the Chancellor's Office to exceed its budget for consulting contracts.

In addition to exceeding certain categories within their budget, the community colleges did not always spend grant funds in compliance with the grant agreements. Specifically, two of the five community colleges we visited inappropriately spent grant funds on projects that were not related to the purpose of the Economic Development grant they had received. For instance, Chaffey College spent approximately $4,000 from its fiscal year 1992-93 Economic Development marketing grant to purchase a computer for its accounting office. According to the dean of economic development at Chaffey College, the college received permission from the Chancellor's Office to purchase the computer. We also determined that Chaffey College spent $65,000 (54 percent) of the $121,086 marketing grant that it received for fiscal year 1992-93 to pay for consulting services from October 1993 to June 1994, even though the grant term ended on September 30, 1993.

Not all grant expenditures were supported in community college accounting records.

We also found that expenditures that were reported in the fiscal reports were not always supported by accounting records at the community colleges. Specifically, for 5 of 12 final fiscal reports that we reviewed, the expenditure amount reported did not agree with the respective community college's accounting records. For example, for fiscal year 1993-94, the amount of expenditures in State Center's accounting records was approximately $3,500 less than what they reported to the Chancellor's Office.

Further, the two grants awarded to El Camino included funding for the National Institute of Standards and Technology program, and its final fiscal reports do not separately identify the amount of Economic Development expenditures. El Camino also does not separately account for Economic Development expenditures in its own accounting records. Therefore, we did not attempt to reconcile the two final fiscal reports submitted by El Camino for fiscal years 1992-93 and 1993-94 to their accounting records for the Economic Development Program. However, we did attempt to determine whether the Economic Development expenditures were appropriately recorded in the accounting records. Based on our review, we determined that El Camino could not identify Economic Development expenditures totaling $26,500 in its fiscal year 1992-93 and $44,100 in its fiscal year 1993-94 accounting records.

Because the Chancellor's Office did not ensure that it received and reviewed the required reports, it was not aware that the community colleges exceeded their line-item budgets without

23

obtaining prior written approval. By not adequately monitoring and reviewing grant expenditures, the Chancellor's Office cannot ensure that the community colleges are spending the grant funds appropriately or that the community colleges are correctly reporting expenditures.

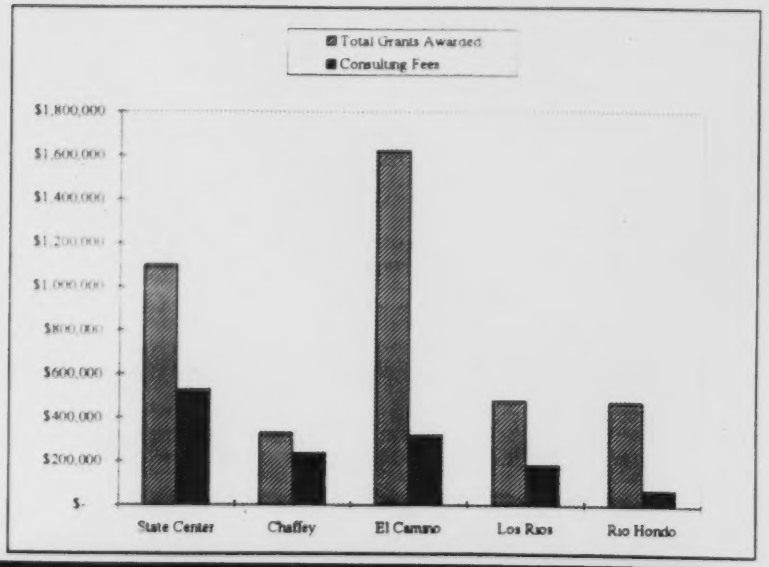
The Use of Consultants by State Center and Chaffey College Was Excessive

While community colleges receive grants for their expertise, many instead hired consultants to do the work.

According to the program specialist for the Economic Development Program, the necessary expertise to effectively administer the program is available at the various community colleges throughout California. Rather than attempt to operate the program at the state level, the Chancellor's Office grants program funds to community colleges that have demonstrated expertise in a particular area of the program. However three of the five community colleges we reviewed spent more than 39 percent of their grant funds on consultants. As noted in Figure 2, during fiscal years 1992-93 and 1993-94, State Center spent approximately $526,169 (48 percent) of the $1,099,286 grant funds it received on consultants. Consultants included the project director, the database manager, and at least 10 employees hired through a temporary personnel agency.

Figure 2

Amount of Grant Funds Awarded and Amount Spent on Consultants Fiscal Years 1992-93 and 1993-94



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The Chancellor's Office also used Chaffey College as a fiscal agent to pay for consultants working at the direction of State Center. Chaffey College received grant funds totaling approximately $330,000 during fiscal years 1992-93 and 1993-94, $237,300 (73 percent) of which was spent on consultants. However, according to the dean of economic development at Chaffey College, all of the consultants worked for State Center in Fresno, and none of them provided any services to Chaffey College. The dean further stated that the college's only responsibility was to pay invoices submitted by the consultants and to prepare the quarterly and final progress reports for the grants. State Center was responsible for developing the grant proposal and selecting the consultants. For its fiscal agent services, Chaffey College received approximately $15,000 in administrative fees during fiscal years 1992-93 and 1993-94.

The use of these consultants directly conflicts with the Chancellor's Office philosophy of distributing funds to community colleges because they have the expertise to operate the programs. We believe that the Chancellor's Office should have awarded the grants to a more qualified college.

Chancellor's Office May Not Be Maximizing Economic Development Grants

Chancellor's Office's policy of extending unspent grant funds denies other colleges the opportunity to obtain grants.

The Chancellor's Office may not be maximizing its use of Economic Development funds. For example, it extended the original grant term to allow the grantee additional time to spend the funds rather than recover unspent grant funds and use them for other Economic Development initiatives. The Economic Development grant agreements specify that funds not spent at the end of the grant period may revert to the State. According to the vice chancellor of the Vocational Education and Economic Development Division, to recover unspent grant funds the Chancellor's Office either bills the entity for the remaining balance of unused funds or, in the case of community college districts funded through the apportionment process, the amount is withheld from future apportionments. Economic Development Program grants may also be amended to extend the time frame for completion of project activities or to allow for new activities. This policy, however, allows the community colleges to retain grant funds for an indefinite period of time, and reduces the incentive for a community college to complete its projects on time. Additionally, the policy denies other community colleges the opportunity to receive grants using unspent grant funds collected by the Chancellor's Office.

During our review of 14 grants at five community colleges, we found five instances where the community college had excess funds at the end of the original grant term. For example, in fiscal year 1992-93, Chaffey College received a grant totaling approximately $121,000. Of this amount, $107,000 (88 percent) remained unspent at June 30, 1993. Rather than reduce the amount of the subsequent year's grant, the Chancellor's Office extended the grant term to September 30, 1993, and Chaffey College used the $107,000 to pay for fiscal year 1993-94 expenditures. The Chancellor's Office awarded Chaffey College approximately $206,000 for its fiscal year 1993-94 grant and did not deduct the $107,000 left over from the previous year. As a result, Chaffey College had not used approximately $143,000 of its fiscal year 1993-94 grant by June 30, 1994. Again, rather than reduce the amount for the next fiscal year's grant, the Chancellor's Office extended the grant term for the fiscal year 1993-94 grant to June 30, 1995.

Los Rios received a grant in fiscal year 1993-94 for approximately $105,000 and had spent only $86,000 by June 30, 1994, the end of the grant term. The Chancellor's Office extended the grant through June 30, 1996, rather than offset subsequent grants awarded to Los Rios. As of June 30, 1995, the $19,000 in excess funds had not yet been used by Los Rios.

The Chancellor's Office Inappropriately Used a Grant Instead of a Contract

Rio Hondo College was awarded grants in fiscal years 1992-93 and 1993-94, each totaling approximately $116,000 to prepare the Economic Development Program Evaluation and Annual Report (annual report). According to the Chancellor's Office's legal counsel, it uses grants to award funds when the activities benefit the local districts and are not defined as a legal responsibility of the Chancellor's Office. Conversely, a contract would be required if the activities are primarily the legal or statutory responsibility of the Chancellor's Office. We asked the legal counsel to review the grants awarded to Rio Hondo College for the annual report to determine whether the use of a grant was appropriate. According to the legal counsel, because the Government Code, Section 15379.23, states that the Board of Governors is to submit an annual report to the governor and the Legislature, the preparation of the annual report is the primary responsibility of the Chancellor's Office. Therefore, the legal counsel concluded that the Chancellor's Office should have used a contract rather than a grant to award the funds to complete the annual report. Because it used a grant, the Chancellor's Office unnecessarily curtailed competition for the

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production of the annual report and Rio Hondo College may not have been the most qualified vendor available to perform the services.

Further, community colleges receive grant funds monthly based on a percentage established by the Chancellor's Office. Because the Chancellor's Office inappropriately used a grant to award the annual report project to Rio Hondo College, the funds were distributed through this apportionment process. As a result, Rio Hondo College received the entire fiscal year 1993-94 grant amount of $116,000 by June 30, 1994, even though the grant did not require the work to be completed until June 30, 1995. If the Chancellor's Office would have used a contract, Rio Hondo College would not have received the funds until the work was complete.

The Chancellor's Office Circumvented the State Budget Process and Incurred Additional Costs

The Chancellor's Office circumvented the state budget process by inappropriately using an interjurisdictional exchange contract. It entered into a contract with State Center in May 1990 to obtain the services of the president of Fresno City College to provide the leadership skills necessary to operate the Economic Development Program. The terms of the contract included a provision that required the Chancellor's Office to pay an automobile and housing allowance to the president. On June 30, 1991, the president resigned from his position at Fresno City College and on July 1, 1991, the former president was officially appointed as the deputy chancellor of the California Community Colleges. However, despite the appointment, the Chancellor's Office executed a second contract with State Center in July 1991 to continue paying the deputy chancellor. The terms of the second contract stated that in addition to providing leadership for the Economic Development Program, the former president would also act as deputy chancellor for the Chancellor's Office of the California Community Colleges. This contract was subsequently amended to continue through June 1994.

By paying its deputy chancellor through a contract with State Center the Chancellor's Office incurred $15,500 of unnecessary costs.

Because the former president was officially appointed as the deputy chancellor in July 1991, the Chancellor's Office should not have awarded the second contract. According to the Chancellor's Office, it continued to pay the deputy chancellor through its contract with State Center so that it could show the related expenditures as contract expenditures rather than personnel service expenditures. However, because it continued to pay the deputy chancellor through the contract with State

Center, the Chancellor's Office incurred unnecessary costs of approximately $15,500 which would not have been paid if it had paid the deputy chancellor through the State's payroll system.

Additionally, the Chancellor's Office created a conflict of interest by allowing the deputy chancellor to approve grants with State Center while continuing to pay him through the contract with State Center. For example, the deputy chancellor approved the fiscal year 1993-94 Economic Development grant awarded to State Center. Although we noted that the grant awarded to State Center included the signature of the vice chancellor of fiscal affairs, because of the deputy chancellor's relationship with State Center, he should not have approved the grants. As a result, the Chancellor's Office risked the possibility that State Center received contracts that it otherwise might not have received.

Corrective Action Taken by the Board of Governors and the Chancellor's Office

The Board of Governors (board) of the California Community Colleges has adopted new policies regarding approval and use of grants and contracts at the Chancellor's Office. In September 1995, the board adopted a policy stating that contracts must be reviewed by the board if amended in such a way as to make them exceed $100,000 or three years in duration, or if they involve consulting services over $50,000. The policy also requires that more complete and timely information be presented to enable the board to decide whether or not to approve contracts. It also requires that the board be given "early warning" about the intent to contract.

Board of Governors has adopted new policies for approval and use of grants and contracts; however, Economic Development Grants are exempt from these new policies.

On November 16, 1995, the board adopted a policy which requires the Chancellor's Office to seek board approval before entering into any grants which exceed $100,000 or three years in duration. The requirement for board approval applies to any amendment that results in the original grant exceeding these limits. The policy also requires that after January 1, 1996, all grants be awarded using either a competitive process or allocation formulas approved by the board. Grants for the performance of functions that are ongoing in nature must be awarded in cycles of one to five years in length. Moreover, the policy requires that, to the extent that the grantee contracts with a private or public entity to perform certain parts of the grant, the grantee shall be required to disclose the intended purpose

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and amount of such subcontracting, agree to follow locally applicable competitive bidding processes in doing such subcontracting, and agree to name the subcontractors chosen.

Although the revised policy improves control over the process for awarding grants, it includes a provision that states that the new procedures shall not apply to grants distributed on an allocation formula basis that has been reviewed and approved by the board. However, since many of the grants awarded by the Chancellor's Office are distributed based on an allocation formula basis, including grants for the Economic Development Program, this provision would result in those grants being exempt from the revised board policies. Therefore, the board should reconsider the provision in its policy that excludes these grants.

In addition, the Chancellor's Office has created a Grants and Contracts processing unit as part of the Fiscal Division. This unit processes grant awards, verifies and logs quarterly and final fiscal reports, reconciles fiscal data with the accounting unit, and maintains the master files for audit purposes. Specialists in the Economic Development and Vocational Education Division monitor the programmatic aspects of the grants.

Conclusion

The Chancellor's Office did not maintain adequate control over its Economic Development Program. Specifically, the Chancellor's Office did not always use a competitive bid process to award Economic Development funds to community colleges, as its policy requires. Therefore, the Chancellor's Office cannot ensure that the most qualified colleges received the funds. The Chancellor's Office also did not adequately monitor and review grant expenditures. As a result, the community colleges did not always comply with the grant requirements. For example, the community colleges did not always provide matching funds in an amount equal to the grant funds, as required, and did not always spend funds in accordance with the approved grant budget. We also noted that the Chancellor's Office inappropriately used a community college as a fiscal agent to pay consultants who were working at the direction of another community college. Finally, the Chancellor's Office circumvented the State's budget process and incurred additional costs because of its inappropriate use of an interjurisdictional exchange contract.

Recommendations

To properly administer the Economic Development Program and control funds for the program, the Chancellor's Office should:

- Ensure that it complies with its policy by using a competitive process to award Economic Development grants;

- Monitor and review grant expenditures to ensure that funds are being spent in accordance with the grant requirements. Procedures should include reviewing reports submitted by community colleges, performing periodic site visits to review supporting documentation for expenditures and matching information, and reemphasizing grant requirements to the community colleges;

- Require the community colleges to use a competitive process to award subcontracts;

- Modify the terms and conditions of the grants to restrict travel costs to state per diem rates;

- Ensure that it follows its own procedures by using contracts rather than grants to award funds when it has the legal or statutory responsibility to perform the activities; and

- Implement procedures to ensure that it is maximizing the use of Economic Development funds. Specifically, the Chancellor's Office should consider reducing the amount of grant funds awarded to community colleges by the amount of unspent funds remaining from prior grants.

Finally, the Chancellor's Office should reimburse the State for the amount of unnecessary costs incurred from its inappropriate use of an interjurisdictional exchange contract.

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Chapter 2

The Chancellor's Office and the Department of Education Used Fiscal Agents To Circumvent State Controls To Develop the State Plan

Chapter Summary

Both the Chancellor's Office of the California Community Colleges (Chancellor's Office) and the Department of Education (department) circumvented state controls by using fiscal agents to obtain the services of a contractor, The Resource Group (contractor), to prepare the Needs Assessment and State Plan for Vocational Education. Specifically, the Chancellor's Office awarded a contract for $220,000 to Chaffey College with the stipulation that the community college use the funds to pay the contractor and also directed Monterey Peninsula College to issue a $43,643 payment to the contractor. Similarly, the department awarded a $300,000 contract to the Los Rios Community College District (Los Rios) and a $300,000 grant to East San Gabriel Valley Regional Occupation Program (East San Gabriel) with the understanding that these entities would use the funds to pay the contractor. By using the fiscal agents, the Chancellor's Office and the department incurred an additional $62,000 in administrative costs that were paid to the fiscal agents. Further, expenditures of approximately $805,000 were not subjected to the State's normal review and internal controls.

The Chancellor's Office and the department submitted documents to the Department of General Services (DGS) that contained misleading information as support for requests for approval of contracts and contract amendments. Furthermore, the Chancellor's Office allowed the contractor to begin work on the state plan before DGS had approved its contract, and the department allowed the contractor to perform services without any formal agreement with either the department or its fiscal agent. Finally, because they used fiscal agents to pay the contractor, the Chancellor's Office and the department had no assurance that the amounts paid to the contractor were appropriate. Appendix B presents a chronology of activities related to the development of the Needs Assessment and State Plan for Vocational Education.

Background

The State of California receives funding for vocational education programs from the federal government under the Carl D. Perkins Vocational and Applied Technology Education Act of 1990 (Perkins Act). The department and the Chancellor's Office use the funds to develop and expand the academic and vocational skills of students in grades K-12 and at the community colleges. During fiscal year 1993-94, the State received $108 million in vocational education funds.

The Code of Federal Regulations, Title 34, Section 403.30, requires the State to submit a Vocational Education State Plan (state plan) that outlines the objectives and activities of its vocational education programs. Section 403.32(b) requires the State to include an assessment of its vocational education programs as part of the state plan. This assessment is designed to demonstrate the need for vocational education and the activities planned to meet those needs. The results of the assessment are to be the basis for completing the state plan.

Since both the department and the Chancellor's Office receive funds to administer vocational education programs in the State, the State Board of Education and the Board of Governors for the California Community Colleges developed a Memorandum of Understanding that delineates the roles and responsibilities of the two agencies as they pertain to the administration and operation of vocational education program services. A description of the process that the two agencies should follow to develop the state plan is included in the Memorandum of Understanding.

In March 1993, representatives of the Chancellor's Office and the department met with the contractor's president to discuss the needs assessment for California's Vocational Education programs. On March 25, 1993, the contractor's president submitted a memorandum to the representatives of both agencies proposing a workplan and budget for completing the needs assessment. The workplan outlined seven major objectives and a projected budget of $335,000. The president also stated that both agencies must be willing to commit to a start date of April 1, 1993, to complete the project by the end of September. On March 31, 1993, the assistant superintendent and state director for the Career-Vocational Education Division of the department notified the contractor that both the department and the Chancellor's Office wished to obtain its services to perform the needs assessment.

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The Chancellor's Office and the Department Used Fiscal Agents To Circumvent State Contracting Requirements

The Chancellor's Office used Chaffey College and Monterey Peninsula College as fiscal agents to obtain the services of the contractor for the work it performed on the needs assessment. Fiscal agents are not subject to state controls. By using fiscal agents, departments can specify the use of funds without subjecting them to state review or oversight. According to the dean of economic development at Chaffey College, the vice chancellor of the Vocational Education Division in the Chancellor's Office asked him if Chaffey College would enter into a $220,000 contract and use the funds to pay the contractor for its work on the Vocational Education needs assessment. Chaffey College agreed to act as the fiscal agent and in August 1993 executed a consultant services agreement with the contractor. Chaffey College paid the contractor $211,540 and retained the remaining $8,460 as an administrative fee.

By using fiscal agents, departments can specify use of funds without subjecting them to state review or oversight.

In May 1993, the Chancellor's Office directed Monterey Peninsula College to pay the contractor $43,643 using funds from a $110,000 contract it had awarded to the college in November 1992. The purpose of the contract was for Monterey Peninsula College to provide technical support for planning, assessment, development of standards and measures of performance, and priority-setting activities to assist the Chancellor's Office to meet the requirements of the Perkins Act. Since the indirect cost for the contract was 8 percent, we determined that the administrative fee for Monterey Peninsula College to issue the payment to the contractor was approximately $3,500.

The department also used fiscal agents to obtain the services of a contractor. Specifically, it awarded a $300,000 contract to Los Rios with the understanding that Los Rios would use the funds to pay the contractor for the needs assessment. According to the project director, who is an employee of Los Rios, he prepared requisitions for payments that the district made to the contractor at the direction of the department. During our review, we noted that the contractor sent two invoices directly to the department rather than to Los Rios. The department forwarded these invoices to Los Rios for payment. In total, Los Rios paid the contractor $275,000 and retained $25,000 as its administrative fee.

The department also awarded a grant totaling $300,000 to East San Gabriel. The superintendent of East San Gabriel stated that in March 1994 the department asked East San Gabriel to apply for funds for the development of the state plan under the Perkins Act. The superintendent further stated that the department asked East San Gabriel to use the grant funds to subcontract the work to the contractor. Finally, the superintendent stated that East San Gabriel did not have any role in selecting the contractor. Of the $300,000 that it received from the department, East San Gabriel paid the contractor $275,000 and retained the remaining $25,000 as its administrative fee.

In total, the State paid fiscal agents nearly $62,000 to issue 12 checks to one contractor.

By using fiscal agents to pay the contractor, the department incurred additional administrative costs of $50,000. While we recognize that the department would have incurred administrative costs had it paid the contractor directly, we question whether those costs would have totaled $50,000. While Los Rios and East San Gabriel issued a total of seven payments to the contractor, the department issued six payments to the fiscal agents, four to Los Rios and two to East San Gabriel. Since the department incurred costs to administer its agreements with the fiscal agents and to issue six payments to them, we do not believe that the department would have incurred the additional $50,000 in administrative costs that it paid to the fiscal agents had it contracted directly with the contractor.

The Public Contract Code, Section 10380, states that DGS is responsible for determining the conditions under which a contract may be awarded without competition and the methods and criteria that must be used to determine the reasonableness of the contract costs. The State Administrative Manual (SAM), Section 1236, states that contracts may be awarded without competitive bids or proposals if DGS agrees that there is only a single source for the services. Section 1236 further states that agencies must submit an application for sole-source exemption that includes a market survey and justification of contract costs. The Public Contract Code, Section 10373, requires state agencies to secure at least three competitive bids or proposals for each consulting services contract. However, the section also states that the work or services of a state or local agency, such as a community college, are specifically exempt from the requirement of acquiring competitive bids.

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By using the community colleges as fiscal agents, the Chancellor's Office and the department circumvented state controls to obtain the services of a specific contractor. Although DGS approved the department's contract with Los Rios, the terms of the contract indicated that the community

college district was to perform the work. By contracting with Los Rios, the department was able to select the contractor without obtaining approval of a sole-source contract from DGS.

The Chancellor's Office and the department paid nearly $62,000 in administrative costs in addition to the $805,000 that the fiscal agents paid to the contractor on behalf of the two agencies. By circumventing the competitive bidding process, the two agencies cannot assure that they used the most qualified contractor or that the amount paid to the contractor was reasonable.

Chancellor's Office's and Department of Education's Use of Fiscal Agents May Have Created Conflicts of Interest

By using fiscal agents, the Chancellor's Office and the department may have caused employees at Chaffey College and at East San Gabriel to violate the common law doctrine against conflicts of interest. For example, by reviewing a sample of "Statements of Economic Interests" for key personnel at the Chancellor's Office, the department, and the community colleges, we determined that the dean of economic development at Chaffey College had worked as a consultant for the contractor during calendar year 1992. In August 1993, Chaffey College entered into a consultant services agreement for which it paid the contractor $211,540. In addition, our review of the workplan the contractor prepared for the department disclosed that the superintendent of East San Gabriel was listed as a consultant to the contractor.

As previously discussed, the Chancellor's Office awarded a contract for $220,000 to Chaffey College with the stipulation that the college use the funds to pay the contractor. The dean of economic development at Chaffey College was named in the contract as the project director. During our review of invoices and requisitions for payment at Chaffey College, we noted that the dean of economic development approved all the payments the college made to the contractor. The dean of economic development had worked as a consultant for the contractor in 1992 and he approved all the payments that Chaffey College made to the contractor for a contract that it awarded to the contractor in August 1993. Therefore, we believe the Chancellor's Office's use of Chaffey College as a fiscal agent may have caused him to violate the common law doctrine against conflicts of interest. We also noted that the president of The Resource Group was a member of the Community Advisory Committee for Chaffey College's Economic Development Center.

The contractor listed the superintendent of East San Gabriel as an employee in the packet it submitted to the department outlining the scope of work for the state plan. The superintendent stated that she worked for the contractor drafting a portion of the state plan and informed the department of this fact in December 1993. Regardless, at the request of the department, in April 1994, only four months after she had worked for the contractor, the superintendent entered into an Educational Services Agreement with the contractor for preparation of the state plan. The agreement stated that the department designated East San Gabriel as the fiscal agent for the project, that all funds for the project would be allocated to East San Gabriel, and that East San Gabriel would forward funds to the contractor. All the invoices the contractor submitted for payment were addressed to the superintendent. We believe that, because the superintendent worked for the contractor just prior to entering into a contract with them, the department may have caused her to violate the common law doctrine against conflicts of interest.

According to the California Attorney General's Office, conflicts of interest by public officials can violate both common law and statutory prohibitions. Common law is a body of law that has been made by precedential court decisions. The basic prohibition in the common law is that a public officer is impliedly bound to exercise powers conferred on him with disinterested skill, zeal, and diligence, and primarily for the benefit of the public. In addition, a California Attorney General Opinion states that the fundamental policy is that a public office is a public trust created in the interest and for the benefit of the people; therefore, public officers are obliged to discharge their responsibilities with integrity and fidelity. Although the employees at Chaffey College and East San Gabriel did not violate any statutory prohibitions, because they both had recently worked for the contractor, they lacked the independence necessary to ensure that the best interests of the State are protected; therefore, they may have violated the common law doctrine against conflicts of interest.

The Chancellor's Office Submitted Erroneous and Misleading Information to the Department of General Services

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In February 1994, the Chancellor's Office awarded a contract totaling $220,000 to Chaffey College to prepare the needs assessment. According to the contract budget, Chaffey College could subcontract out $66,000 of the work. The staff counsel at DGS, who reviewed the contract in January 1994, raised concerns about the amount of work to be subcontracted out.

Additionally, she inquired about whether Chaffey College intended to use a competitive bid process to award the subcontracts. In a memorandum to DGS dated February 14, 1994, the Chancellor's Office stated that the subcontracts were necessary to have access to a proprietary data base developed by the contractor. The Chancellor's Office also stated that the policy at Chaffey College requires contracts exceeding $25,000 to be competitively bid. The Chancellor's Office further stated that since Chaffey College had an existing contract with the contractor for an amount less than $25,000 and because funds from the Chancellor's Office contract would be used to augment the existing contract, competitive bidding by Chaffey College was not required. DGS approved the contract on February 23, 1994.

We reviewed both the contract between the Chancellor's Office and Chaffey College and the contract between Chaffey College and the contractor. In August 1993, Chaffey College awarded a contract totaling $167,600 to the contractor to prepare the needs assessment. According to the dean of economic development at Chaffey College, the contract was awarded to the contractor at the request of the vice chancellor of the Vocational Education Division in the Chancellor's Office. The dean of economic development also stated that Chaffey College awarded the contract based on verbal approval from the vice chancellor that the Chancellor's Office would award a contract to Chaffey College to pay for the subcontract. On February 22, 1994, at the direction of the vice chancellor, Chaffey College increased the amount of its contract with the contractor by $42,847.

Despite knowing that subcontractors had already been paid $168,693, the Chancellor's Office submitted a contract to DGS indicating that payments to subcontractors would not exceed $66,000.

By December 1993, Chaffey College had already paid the contractor $168,693 for work on the needs assessment. This amount included a finance charge of $1,093 due to late payment. On February 18, 1994, the contractor submitted an additional invoice for $42,847 to Chaffey College. When the Chancellor's Office submitted its contract to DGS in January 1994 to reimburse Chaffey College, it had full knowledge that $168,693 had been paid to the contractor. Therefore, the Chancellor's Office submitted erroneous information to DGS by stating in the contract budget that the amount to be paid to subcontractors would not exceed $66,000.

In early February 1994, the vice chancellor of the Vocational Education Division sent a memorandum to the contracts manager for the Chancellor's Office requesting an augmentation of the contract with Chaffey College. She stated in her memorandum that when she received the State Plan Guide from the U. S. Department of Education (USDE) in November 1993, she realized the process to complete the state plan had only

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begun and the Chancellor's Office did not have sufficient resources to complete it by the federal deadline. Consequently, she asked Chaffey College to determine whether the contractor could be retained to complete the state plan. She further indicated that by the end of December 1993, the contractor had prepared a draft copy of the state plan and distributed copies of it throughout the State. She stated that the contractor was currently in the process of revising the state plan based on comments received at public hearings. She concluded her memorandum by stating that, without the help of Chaffey College and the contractor, the vocational education funds for the State would have been jeopardized; however, the project had a cost overrun of approximately $400,000. As a result, the Chancellor's Office needed to provide the funds to pay the contractor for the work it had already done on the state plan and for revising and submitting it to the USDE before May 1, 1994.

On the advice of its legal unit, the Chancellor's Office decided to pursue approval of a sole-source contract with the contractor rather than amend its existing contract with Chaffey College. On March 25, 1994, the Chancellor's Office submitted a request to DGS seeking approval of a $400,000 sole-source contract with the contractor. In its request, the Chancellor's Office stated that the purpose of the sole-source contract was to obtain the professional services of the contractor to develop, revise, and submit the state plan to the USDE on or before May 1, 1994. As required by the SAM, Section 1236, the Chancellor's Office submitted a Request for Exemption From Competitive Bidding that included a justification for the sole-source contract. The Chancellor's Office also included a copy of a market survey to document its attempts to identify other firms that could provide the services. At the request of DGS, the Chancellor's Office made revisions to the contract, and it was approved on May 16, 1994.

We determined that, because the Chancellor's Office did not disclose to DGS that the contractor had already completed a substantial portion of the state plan, the information in its justification for the sole-source contract was misleading. The justification submitted on March 25, 1994, stated that time constraints required the Chancellor's Office to obtain the professional services of a firm that has the experience and expertise to complete the state plan accurately and on time. While work had been ongoing within the Chancellor's Office since October 1993, according to the justification, it could not meet the May 1, 1994, deadline without external professional services. As previously mentioned, the contractor actually started working on the state plan as early as November 1993 and delivered a draft copy of the state plan to the Chancellor's

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Office on January 3, 1994, nearly three months prior to the date the Chancellor's Office submitted its request for the sole-source contract to DGS.

The Chancellor's Office requested approval of a $400,000 sole-source contract nearly three months after the contractor had completed a draft copy of the state plan.

We also determined that the vice chancellor of the Vocational Education Division conducted the market survey component of the sole-source justification after the vendor had already been selected and had begun work on the state plan. In addition, in the portion of the sole source justification that documented the market survey, the Chancellor's Office stated that it was unable to identify another firm that had the knowledge and experience or the time and resources required to complete the state plan under the extremely tight time constraints. However, in the memorandum she sent to the contracts manager in February 1994, the vice chancellor wrote that in November 1993 she had asked Chaffey College if the contractor could prepare the state plan. Because the Chancellor's Office had already selected a vendor and the draft had been delivered to the Chancellor's Office on January 3, 1994, the market survey that it submitted to DGS on March 25, 1994, was irrelevant.

In the contract that it submitted to DGS, the Chancellor's Office indicated that the term would be March 30, 1994, through August 31, 1994, even though it had already received the draft copy of the state plan. Therefore, the Chancellor's Office requested approval of the sole-source contract with full knowledge that the contractor had already been working on the state plan. Although minor revisions were made to the state plan in June 1994, a draft copy was actually sent to the USDE on April 12, 1994. When the Chancellor's Office submitted its request for approval of the sole-source contract on March 30, 1994, it was aware that the contractor had nearly completed the project and the information submitted with the sole-source justification was misleading.

The Department of Education Submitted Misleading Information to DGS but Subsequently Withdrew Its Request for Approval of a Contract Amendment

The department also submitted misleading information to DGS in an attempt to amend an existing contract that it had with Los Rios. In its request, the department stated that the purpose of augmenting the contract was to add $432,000 to fund a set of activities and deliverables necessary to complete the state plan. However, the staff counsel at DGS raised several concerns regarding the amendment, and the department subsequently withdrew its request.

Specifically, the department submitted its request for the amendment to DGS on January 31, 1994, even though it had already received a draft of the state plan on January 3, 1994. On February 14, 1994, the DGS staff counsel who reviewed the request asked the department to clarify certain provisions in the amendment. The staff counsel asked the department to explain why all of the additional funding was budgeted for subcontractors and why it needed to contract with Los Rios if the district was not doing the bulk of the work. The staff counsel also asked the department to explain how Los Rios selected the subcontractors. On March 7, 1994, the department submitted additional information to DGS describing the purpose of the contract amendment; however, the staff counsel still expressed reservations regarding the amendment. On April 6, 1994, the department withdrew the amendment. On April 12, 1994, six days later, the department awarded a $300,000 grant to East San Gabriel and submitted a draft copy of the state plan to the USDE. According to the superintendent of East San Gabriel, the department asked it to use the grant funds to pay the contractor for the state plan.

When it submitted its request for a contract amendment, the department failed to inform DGS that the contractor had been working on the state plan for more than three months.

We also noted that on October 21, 1993, the department received an invoice from the contractor for work it had done on the state plan. The department forwarded the invoice to Los Rios and directed the district to pay it. The district paid the $100,000 invoice on November 5, 1993. Because the department received an invoice from the contractor in October 1993 for work done on the state plan and because it received a draft copy of the state plan from the contractor on January 3, 1994, we believe the department had clearly directed the contractor to work on the state plan before it submitted its request for the amendment to DGS on January 31, 1994. Despite the fact that the department withdrew the amendment, we found that the information the department submitted to DGS was misleading.

Knowingly misrepresenting the facts in a contract or a contract amendment is a violation of law. Specifically, the Government Code, Section 6203, states that officers authorized by law to make or give any certificate or other writing are guilty of a misdemeanor if they make and deliver as true any certificate or writing containing statements that the officers know to be false.

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The Department of Education and the Chancellor's Office Cannot Assure That Payments for Projects Were Appropriate or Reasonable

Because they used fiscal agents to pay the contractor, both the department and the Chancellor's Office lacked control over the payments made for the needs assessment and the state plan. As Table 4 shows, the projected budget for the needs assessment was $335,000; however, the two agencies paid the contractor $430,183 for the project. The two agencies paid $775,000 to the contractor for the state plan even though in its proposals, the contractor stated that it would charge a fixed fee of $750,000. Because the contractor submitted most of the invoices to the fiscal agents, neither the department nor the Chancellor's Office can assure that they received the services they paid for, nor can they assure that the costs they paid for the services were reasonable.

Table 4

Budgeted Amounts for Needs Assessment and State Plan and Amounts Paid to Contractors

Department	Project	Budgeted Cost	Amount Paid to the Contractor	Amount Over Budget
Chancellor's Office	Needs assessment	$ 167,500	$ 260,183	$ 92,683
Department of Education	Needs assessment	167,500	170,000	2,500
Subtotal		335,000	430,183	95,183
Chancellor's Office	State plan	400,000	400,000	0
Department of Education	State plan	350,000	375,000	25,000
Subtotal		750,000	775,000	25,000
Total Costs		**$1,085,000**	**$1,205,183**	**$120,183**

For example, the $260,183 that the Chancellor's Office paid for the needs assessment exceeded the projected budget by $92,683. Three different community college districts paid a portion of this total; Chaffey College paid $211,540, Monterey Peninsula paid $43,643, and Los Rios paid $5,000. As stated earlier, the Chancellor's Office asked Chaffey College to enter into a contract with the stipulation that the community college use the funds to pay the contractor and directed Monterey Peninsula to issue the $43,643 payment to the contractor.

Los Rios used $5,000 from a contract that the Chancellor's Office had awarded it to pay an invoice from the contractor. However, the invoice represented charges for services that the contractor performed on behalf of the department, not the Chancellor's Office. Therefore, the Chancellor's Office paid for a portion of the department's costs for the needs assessment. Because the Chancellor's Office used fiscal agents to pay the contractor for the needs assessment, the payments were not subjected to objective review by the fiscal agents nor to the State's normal review, such as that by the State Controller's Office, the Department of General Services, and other fiscal and contracting controls it must follow when processing payments through its own accounting office. Therefore, the Chancellor's Office cannot assure that it received the services it paid for, nor can it assure that the costs paid for the services were reasonable.

Chaffey College cannot assure that it did not pay for the same services twice.

In addition to the amount by which the payments exceeded the projected budget, we also determined that the Chancellor's Office may have paid for the same services more than once. During our review of invoices the contractor submitted to Chaffey College for the needs assessment, we identified two for which the contractor included charges for the same activities. Specifically, the contractor submitted an invoice totaling $50,000 to Chaffey College on October 2, 1993, and on October 22, 1993, it submitted another invoice for $36,243. Some of the activities listed on the second invoice were the same activities listed on the October 2, 1993, invoice. Because Chaffey College paid the second invoice in full without questioning whether it had already paid for some of the activities listed on the invoice, it cannot assure that it had not paid for the same services twice.

The Department of Education and the Chancellor's Office Allowed the Contractor To Commence Work Prior to Approval of Their Agreements

The department authorized the contractor to begin working on the needs assessment while it arranged an agreement with Los Rios to pay for the work. It did not ensure that Los Rios executed a formal contract with the contractor. Furthermore, while it was still in the process of preparing a contract with Los Rios, the department instructed the district to pay the contractor using funds from another contract that the district had received from the department.

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During our review of payments that Los Rios made to the contractor, we noted that it issued the first payment, totaling $50,000, on June 10, 1993. The department did not issue a contract to Los Rios for the needs assessment until September 17, 1993. Representatives of Los Rios stated that the department directed the district to use funds from a Tech-Prep contract to pay the contractor until DGS approved the contract. After DGS approved the contract that the department intended to award to Los Rios to pay for the needs assessment, the district issued three more payments to the contractor totaling $220,000. However, even though the department awarded the contract to Los Rios with the stipulation that the district use the funds to pay the contractor for the needs assessment, neither the department nor the district had any type of contractual agreement with the contractor. By permitting Los Rios to issue progress payments without the benefit of a formal contract, the department created a risk that public funds would be gifted should the contractor fail to complete the needs assessment.

The Chancellor's Office also allowed the contractor to commence work prior to approval of its sole-source contract. In March 1994, the Chancellor's Office elected to pursue approval of a sole-source contract with the contractor for $400,000 for the state plan. Although DGS did not approve the contract until May 16, 1994, the Chancellor's Office allowed the contractor to begin working on the state plan as early as November 1993. We noted that the contractor submitted its first invoice, totaling $284,500, to the Chancellor's Office on May 17, 1994, one day after DGS approved the sole-source contract. As discussed earlier, the contractor submitted a draft copy of the state plan to both the Chancellor's Office and the department on January 3, 1994, and a revised draft of the state plan was submitted to the USDE on April 12, 1994.

The contractor submitted an invoice for $284,500 to the Chancellor's Office one day after DGS approved the sole-source contract.

Although minor revisions were made to the state plan in June 1994, by June 3, 1994, the contractor had billed a total of $725,000 (94 percent) of the $775,000 that the department and the Chancellor's Office paid for work on the state plan. Therefore, the contractor had completed a substantial portion of the work on the state plan before June 1994.

By allowing the contractor to begin work before approval of the contracts, both the department and the Chancellor's Office exposed the State to potential monetary liability. In addition, by permitting Los Rios to issue progress payments to the contractor without the benefit of a formal contract, the department created a risk that public funds would be gifted should the contractor fail to complete the work.

The Public Contract Code, Section 10360, states that consulting services contracts are not effective until approved by DGS. In addition, Section 10371 states that, except in an emergency, consulting services contracts must not begin prior to formal approval by DGS and no payments can be made before approval of the contract. Further, the SAM, Section 1209, states that agencies must submit each contract to DGS early enough to allow DGS sufficient time to review and comment on the contract prior to the commencement of work.

According to the Chancellor's Office, the tight time constraints, lack of staff, and lack of internal expertise precluded it from completing the needs assessment and the state plan internally; therefore, they had to seek outside help. The department stated that field concerns over the lack of participation by service providers and practitioners in the development of the 1991 plan required the department and the Chancellor's Office to establish a broadly collaborative, statewide development process. The department further stated that this monumental coordination effort necessitated the use of professional services with expertise to complete the projects in a timely manner.

Both agencies contend that they used fiscal agents to assure that the state plan was submitted on time rather than jeopardize $250 million in federal funds.

However, we believe they had sufficient time to develop the plan without violating state contracting procedures.

Both agencies also indicated that the state plan submitted in 1991 had significant problems which resulted in funding being delayed to California; therefore, they wanted to make sure the state plan for 1994-96 was accurate, complete, and in the proper format. The agencies stated that failure to meet the May 1, 1994, deadline would jeopardize nearly $250 million in federal vocational education funds for California.

Although we agree that the preparation of the state plan is a complex project that requires a large investment of time and resources, we believe that if the two agencies had begun the process of developing the state plan earlier, they could have met the deadline for submitting the plan to the USDE without violating state contracting procedures. Both agencies knew that the state plan for 1994-96 had to be submitted to the USDE by May 1, 1994. The Code of Federal Regulations, Title 34, Section 403.33(c), states that the final state plan must be submitted to the USDE by May 1 of the year preceding the first fiscal year the plan is to be in effect. In addition, Section 403.30 requires states that wish to participate in the State Vocational and Applied Technology Program to submit an initial state plan covering a three-year period and subsequent plans to cover two years. California submitted its initial state plan, covering fiscal years 1991-92 through 1993-94, to the USDE in 1991; therefore, the subsequent plan would cover fiscal years 1994-95 and 1995-96.

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Since the same two agencies prepared and submitted the initial state plan in 1991, they had experience in preparing it and could have started the planning process for the 1994-96 state plan early enough to allow adequate time for completion. In addition, the Memorandum of Understanding between the two agencies that describes the process for developing the state plan specifically states that to meet the May 1 deadline, the process must begin 18 to 24 months prior to the deadline.

In addition to time constraints, the Chancellor's Office stated that the USDE did not distribute the final draft of the State Plan Guide and State Plan Checksheet to states until February 22, 1994; therefore, it had to get a substantial amount of work done in a short period of time. However, the transmittal memorandum that the USDE sent with the State Plan Guide and State Plan Checksheet pointed out that it had sponsored four workshops in the fall of 1993 where earlier drafts of the documents were made available to the participants. The USDE also stated that the most significant changes would be in the State Plan Checksheet, which is an internal document used by the USDE when it reviews state plans. The USDE said the checksheet was provided to the states as a courtesy and not as guiding information to develop their plan. The State Plan Guide lists the regulations that must be addressed in the state plan, and only minor changes were being made to it.

Corrective Action Taken by the Department of Education

The Superintendent of Public Instruction has implemented new policies regarding approval and use of contracts at the department. Specifically, in January 1995, the superintendent issued a policy stating that effective immediately the superintendent will review all proposed contracts. In addition, she stated that requests to extend contracts beyond the original ending date must be accompanied by a full explanation of the reason for the extension and a summary of the work completed to date. The superintendent also stated that effective April 1, 1995, contracts not fully executed by the starting date will receive personal review by the superintendent as to the reasons for the delay. Furthermore, she discouraged the use of sole-source contracts, stating that any requests for such contracts will be closely reviewed and approved by her. Finally, the superintendent stated that it will no longer be acceptable to circumvent appropriate contracting procedures through Budget Act language that mandates a specific contractor.

Effective January 1995, the Superintendent of Public Instruction's policy is to review all proposed contracts.

Conclusion

The Chancellor's Office and the department circumvented state controls by using Los Rios and East San Gabriel, Monterey Peninsula College, and Chaffey College as fiscal agents to obtain the services of a contractor to prepare the needs assessment and state plan for Vocational Education. Because they used fiscal agents to circumvent state contracting procedures, the Chancellor's Office and the department paid $62,000 in administrative fees in addition to the amounts they paid to the contractor.

The Chancellor's Office and the department submitted documents that included erroneous and misleading information to DGS as support for requests for approval of contracts and amendments. In two instances, employees at two of the entities used as fiscal agents had recently been employed by the contractor and therefore the Chancellor's Office and the department may have caused them to violate the common law doctrine against conflicts of interest. Because they used fiscal agents to pay the contractor, both the Chancellor's Office and the department lacked control over payments made for the needs assessment and the state plan. As a result, the Chancellor's Office and the department cannot assure that the amounts they paid for the needs assessment and the state plan were appropriate or reasonable.

Recommendations

The Chancellor's Office and the department should:

- Discontinue the use of fiscal agents to circumvent state controls;
- Comply with state requirements for awarding contracts and submit complete, accurate information to DGS when requesting approval of contracts;
- Ensure that DGS has approved its contracts before allowing contractors to commence work; and
- Determine whether the amounts paid to the contractor for the needs assessment and the state plan were appropriate and, if necessary, recover any overpayments.

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We conducted this review under the authority vested in the state auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope of this report.

Respectfully submitted,

Kurt Sjoberg

KURT R. SJOBERG
State Auditor

Date: January 4, 1996

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Appendix A

Description of Economic Development Program Initiatives Funded by the Chancellor's Office

In 1988, the Chancellor's Office established the Economic Development Program to support local community colleges' efforts to provide education, training, and technical services to California business and industry. In fiscal year 1993-94, the program was divided into 15 categories: 8 continuing initiatives and 7 annual initiatives. The difference between the two types of initiatives is that annual initiatives must be competitively bid every year while continuing initiatives must only be competitively bid in the first year of the award. Thereafter, participating community colleges continue to receive the funds for that particular initiative as long as the prior year's work is satisfactory. During fiscal year 1993-94, the Chancellor's Office awarded 53 grants for continuing programs and 53 for annual programs. Descriptions of the various program initiatives are presented below.

Continuing Program Funding Categories

Statewide Coordination Network (ED-Net)

This program provides operational, technical, logistical, and marketing support for all of the Economic Development programs. The network includes a database and electronic bulletin board that provide program support and help to disseminate information on services available to business and industry. In addition, the network acts as a central contact for businesses to identify resources and services available at the community colleges and to determine their training needs.

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Small Business Development Centers

These centers provide comprehensive services to small business owners and to individuals interested in starting their own businesses. For example, the centers act as information, resource, and referral agencies, and they provide training workshops and classes for owners of small businesses.

Centers for Applied Competitive Technologies

These centers help small- and medium-sized businesses evaluate their readiness for new technology and design a business plan. The centers deal with computer-integrated manufacturing, total quality management, and the use of technology transfer teams. These centers provide training in cooperation with the California Manufacturing Technology Center located at El Camino College. The primary goals of the centers are to: improve the competitiveness of small- and medium-sized manufacturers, assist in the conversion of defense suppliers to commercial applications, and increase the adoption of environmentally and economically sound manufacturing technologies and techniques.

Centers for International Trade Development

The goals of these centers are to enhance the competitive strength of California businesses in the international marketplace and to support international trade development in their local communities. The community colleges that participate in this program develop courses in international business, identify local businesses interested in international trade development, and provide direct technical support to those businesses.

Workplace Learning Resources Centers

Through these centers, the community colleges provide business and industry with a variety of workplace learning services, such as occupation-specific skills assessment, task analysis, basic skills, English as a second language, analytical and problem solving skills, and teamwork.

Regional Economic Development and Contract Education Support, and In-Service Training Coordination

The goals of this program include: providing regional coordination of economic development programs; improving statewide coordination of contract training; enhancing the technical skills of faculty and staff to assess business needs, market the colleges services, provide training, and develop materials; and developing partnerships, resources, and projects.

Regional Environmental Business Resource and Assistance Center

The center develops, implements, maintains, and coordinates statewide programs and services designed to mitigate the impact of environmental compliance regulations. These regulations specify the manner in which businesses may handle, store, use, and dispose of hazardous materials. The center provides compliance counseling, applied technology counseling, financial counseling, and environmental audit assistance.

Locally-Based Statewide Program Leadership, Coordination, and Technical Assistance

Through this program, the community colleges provide statewide leadership to: build the system's capacity to deliver education, training, and services appropriate to small- and medium-sized businesses; coordinate resources; and provide a systemwide response to economic development opportunities.

Annual Program Funding Categories

Employer-Based Training

The intent of this program is to expand employer-based training by providing funds that are matched from other sources. Proposed projects are designed to assist community colleges in serving businesses to meet new or changing job opportunities and new or emerging technological fields.

Economic Development Training Set-Aside

In cooperation with the California Department of Commerce, the Chancellor's Office sets aside program funds to promote the creation of new businesses in California. Funds are available for training projects that are part of a new business startup, site location, or business expansion. In addition, the funds provide community colleges the flexibility to develop and deliver quality training programs to a business that is creating new jobs.

Vocational Education/Technology Instructor and Career-Counselor In-Service Training

The intent of this program is to increase the effectiveness of vocational education/technology instructors and career counselors and to promote the development of new curricula. Emphasis is placed on those occupations undergoing the most rapid technological changes. Projects funded through this program provide actual hands-on experience at the work site by providing instructors or counselors with a minimum of six weeks of training at a structured work site.

Technical Instructor Intensive In-Service Training

Funds are set aside from the Vocational Education/Technology Instructor and Career-Counselor In-Service Training category above to provide additional projects on a developmental application basis that include an intensive training component prior to the structured 120-hour work site experience.

Environmental Hazardous Materials Technology Training Program

Under this program, community colleges provide a pool of trained technicians who have completed a certificate or associate degree in environmental materials technology. The program helps California industry to comply with state and local regulations on hazardous materials and provides training opportunities for hazardous materials handling within an industry.

Model Community Economic Development Programs

Funds are provided under this program to help community colleges participate in local economic development programs. Regional training sessions are provided to help colleges understand the practical application the model may have for those who wish to replicate all or parts of the model in their region. The resulting products, such as manuals, handbooks, curricula, survey instruments, and project reports, are distributed to all community colleges in the State.

Program Evaluation and Annual Report

These funds provide for an annual performance review and report. The report provides an overview of programs, performance indicators, and results and characteristics of participants.

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Appendix B

Chronology of Key Events in Preparation of the Vocational Education Needs Assessment and State Plan

Date	Department of Education Activity	Chancellor's Office Activity	Description
March 25, 1993	The Resource Group (contractor) submits a memorandum to the Chancellor's Office (office) and the Department of Education (department) proposing a workplan and budget for the needs assessment.		The workplan outlines seven major objectives with a projected budget of $335,000. The contractor indicates that it must begin work by April 1, 1993, to complete the project by the end of September.
March 31, 1993	The department submits a letter to the contractor stating that the department and the office concur that work on the needs assessment must begin immediately and that the two agencies wish to obtain the services of the contractor.		
April 16, 1993	The department instructs the contractor to direct invoices for the needs assessment to the Los Rios Community College District.		
April 29, 1993	The contractor bills the department $50,000 for work on the needs assessment.		
May 10, 1993		The office directs Monterey Peninsula College to pay the contractor $43,643 for work on the needs assessment.	The payment was made from an existing contract the office had with Monterey Peninsula College.
June 10, 1993	The department directs Los Rios to pay the contractor $50,000 for work on the needs assessment. This payment is for the invoice submitted by the contractor on April 29, 1993.		At the direction of the department, the payment was made from an existing Tech-prep contract Los Rios had with the department. However, the needs assessment was not included in the scope of work of this contract. The department did not award a contract to Los Rios for the needs assessment until September 17, 1993.

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Date	Department of Education Activity	Chancellor's Office Activity	Description
August 2, 1993	The contractor submits an invoice for $75,000 to the department for the needs assessment.		
August 20, 1993		At the request of the office, Chaffey College awards a contract totaling $167,600 to the contractor for the needs assessment.	
August 23, 1993		The contractor submits an invoice to Chaffey College for $81,357.	The date of the invoice is only three days after the contract was approved.
September 17, 1993	The department awards a contract to Los Rios for the needs assessment.		The amount of the contract is $300,000.
October 2, 1993	The contractor submits an invoice to Los Rios for $45,000 for work on the needs assessment.	The contractor submits an invoice to Chaffey College for $50,000 for the needs assessment.	
October 21, 1993	The contractor submits an invoice to the department for $100,000 for work on the state plan.		
October 22, 1993		The contractor submits an invoice to Chaffey College for $36,243 for the needs assessment.	
November 1, 1993	The contractor submits an invoice to Los Rios for $5,000 for the needs assessment.		Los Rios uses funds from a contract it received from the office to pay the invoice.
November 5, 1993	At the direction of the department, Los Rios pays the contractor $100,000 for the state plan.		This payment is for the invoice submitted to the department on October 21, 1993. Los Rios inappropriately uses funds from its contract with the department for the needs assessment to pay the contractor for work on the state plan.
January 3, 1994	The contractor submits a draft copy of the state plan to the department.	The contractor submits a draft copy of the state plan to the office.	
January 31, 1994	The department submits a request to the Department of General Services (DGS) to amend the Los Rios contract for the needs assessment from $300,000 to $732,000.		The purpose of the amendment is to fund activities necessary to complete the state plan.

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Date	Department of Education Activity	Chancellor's Office Activity	Description
February 18, 1994		The contractor submits an invoice to Chaffey College for $42,847 for needs assessment	Chaffey College already paid the contractor $168,693, which was the amount of the original contract, and a $1,093 fee for late payments. Therefore, funds do not exist under the contract to pay this invoice.
February 22, 1994		At the request of the office, Chaffey College amends their existing contract with the contractor by $42,847.	
February 23, 1994		The office awards a contract totaling $220,000 to Chaffey College for the needs assessment.	According to the Dean of Economic Development at Chaffey College, the contract is to reimburse Chaffey College for the payments it made to the contractor.
March 7, 1994	At the request of the DGS, the department submits additional information regarding its request to amend the Los Rios contract.		
March 25, 1994		The office submits request for approval of a sole-source contract to the DGS.	The sole source contract, totaling $400,000, is to obtain the services of the contractor. The request includes a market survey and sole-source justification.
April 6, 1994	After additional concerns were raised by the DGS, the department withdraws its request to amend the Los Rios contract.		
April 12, 1994	The department awards a grant totaling $300,000 to East San Gabriel Valley ROP for the state plan.	A draft copy of the state plan is submitted to the U.S. Department of Education.	The department awarded this grant six days after it withdrew its amendment request for the Los Rios contract. The department asks East San Gabriel Valley ROP to use the funds to pay the contractor.
May 1, 1994	The contractor submits an invoice to East San Gabriel Valley ROP for $102,500 for the state plan.		The invoice was paid on May 27, 1994.
May 5, 1994	The contractor submits an invoice to East San Gabriel Valley ROP for $102,500 for the state plan.		The invoice was paid on June 10, 1994.
May 10, 1994	The contractor sbmits an invoice to East San Gabriel Valley ROP for $47,500 for the state plan.		The invoice was paid on June 29, 1994.

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Date	Department of Education Activity	Chancellor's Office Activity	Description
May 16, 1994		The office awards a sole-source contract for $400,000 to the contractor for the state plan	
May 17, 1994	The contractor submits an invoice to East San Gabriel Valley ROP for $22,500 for the state plan	The contractor submits an invoice for $284,500 to the office for the state plan	This invoice was submitted to the office one day after the sole-source contract was awarded. The invoice was paid on July 8, 1994
June 3, 1994		The contractor submits an invoice for $65,500 to the office for the state plan	
June 23, 1994	The department submits a letter to USDE listing minor revisions made to the state plan	The contractor submits an invoice for $50,000 to the office for the state plan	In accordance with the terms of the contract, the office withheld $30,000 for progress payments
October 11, 1994		The contractor submits an invoice for $30,000 to the office for the state plan	

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CHANCELLOR'S OFFICE
CALIFORNIA COMMUNITY COLLEGES
1107 NINTH STREET
SACRAMENTO, CA 95814
(916) 445-8752

January 2, 1996

Kurt R Sjoberg
State Auditor
Bureau of State Audits
660 J. Street, Suite 300
Sacramento, CA 95814

Dear Mr. Sjoberg:

The Chancellor's Office and Board of Governors of the California Community Colleges thank you for the opportunity, albeit brief, to respond to the draft report of the audit (#94-123) conducted by your staff from March 16, 1995 to December 19, 1995. We have reviewed the report and have found much that we agree with; indeed, many of the problems raised in the report have already been identified and corrected through our own existing internal controls and procedures.

In some instances we believe your report uses incomplete information and makes faulty assumptions that lead to incorrect conclusions and wrongfully tarnish the agency and the Board of Governors. We do not wish to dwell on these negatives, but will point out these instances so that the public record on these matters is clear. In addition, the deadline for response during the holiday period has limited our ability to be as responsive as we would have liked. With the colleges closed, and many of our senior staff on vacation, it has been difficult to verify information at both the state and local levels. In light of the fact that you denied our request to delay our response by one week (to January 8th), we hope you'll understand that we must reserve the right to contest your findings and submit additional responses as we continue to verify the accuracy of the information and conclusions contained in the report. (1) (2)

Areas of Agreement

Among the key findings in Chapter 1 of the report is that the Chancellor's Office did not consistently apply its policies which specify the use of a competitive process to award Economic Development grants. In Chapter 2, the report focuses on transactions that surrounded contracting for the Needs Assessment for Vocational Education, and the preparation of the State Plan for Vocational Education. Several weaknesses in the contracting process were identified. We agree these matters are in need of attention;

The California State Auditor's comments on this response begin on page 77

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and, in fact, they have been the subject of our own internal review and improvement procedures. At its September 1995 meeting, the Board of Governors adopted a major revision of its Standing Orders on Contracting (Section 318, copy attached). This revised Standing Order provides more Board oversight of the contracting process and takes steps to ensure that all proposals will be scored in an objective and fair manner. At its November meeting, the Board of Governors adopted a new Standing Order on Grants (Section 319, copy attached). This new Standing Order assures that except in narrow instances, all grants awarded by the Board of Governors will be awarded through competitive processes for fixed periods of time of up to five years. It is our belief that with the adoption of these Standing Orders, the agency is already well underway in addressing many of the concerns that have been brought to light in your report.

Aside from these actions we have already taken, we agree that the Chancellor's Office is not always able to monitor the community colleges to ensure they are complying with grant requirements. We agree that we cannot ensure that every grantee expends funds in accordance with its approved grant budget. We agree that the expenditures recorded in some accounting records do not always agree with the expenditures reported to the Chancellor's Office. We agree that some community colleges do not always provide adequate matching funds; and we agree that some colleges do not obtain approval from the Chancellor's Office prior to awarding subcontracts. As you know, 100% compliance monitoring is beyond the realm of reasonable expectation. During the last four years the Chancellor's Office has lost 40% of its state-funded staff (over 60 full-time positions) and 47% of its state-funded operations budget. We still devote substantial resources to monitoring grants; but to increase our levels of compliance monitoring, we would need additional staff to restore our capability to do such monitoring.

We agree that the Economic Development grants allow the community colleges to reimburse travel costs at district rates, which, in specific instances, may or may not happen to be in excess of the State rates. These grants, however, are in the form of local assistance funds to the colleges; and we thus allow districts the same freedom to expend these revenues that they have with other local assistance revenues. Indeed, since district employees are not State employees, the State reimbursement rates aren't legally applicable. As far as we know, other local assistance allocations made through the state budget process to other agencies of local government do not contain the kind of spending restrictions your report intimates ought to be applied to Economic Development grants to community college districts. At this point, therefore, we cannot accept your recommendation that the terms and conditions of such grants should be modified to restrict travel costs to state per diem rates. (3)

We agree that it was inappropriate to use a grant to Rio Hondo College as a means of preparing the Economic Development Program Evaluation and Annual Report. This activity is something more appropriately part of the legal or statutory responsibility of the Chancellor's Office, and hence, should have been awarded as a contract. Our own

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internal procedures require the Legal Division to review all grants and contracts to assure that they are appropriately classified. At this point in time we have corrected this problem for the future and believe the lack of review on this grant was an isolated instance.

We agree that, in light of all facts and circumstances, the $220,000 contract with Chaffey College to prepare the Needs Assessment for the State Plan for Vocational Education was a "fiscal agent" contract, and that the Chancellor's Office should have either competitively bid the project or sought and obtained sole source approval to contract directly with The Resource Group. Through our own internal controls and procedures, we reviewed the grant (for fiscal year 1993-94) that had been given to Chaffey College for the Needs Assessment. We required, in October of 1993, that the grant be withdrawn, and that the transaction proceed as a contract, including review and approval by the Department of General Services. The detailed supporting materials we submitted to General Services regarding this contract indicated that $66,000 of the contract amount would be subcontracted. We had no intent to mislead the Department of General Services, and regret that we may have unknowingly passed along inaccurate information to that agency. (4)

We agree, and my key staff were aware at the time, that The Resource Group commenced performance on the State Plan for Vocational Education before General Services and the Board of Governors approved the sole source contract. Compelling circumstances involving an impossible timeline and the possible loss of hundreds of millions of dollars in federal funding for the colleges encouraged us to take this step.

Areas of Disagreement

We disagree that the Chancellor's Office circumvented the state budget process by paying the salary of its deputy chancellor through a contract with State Center Community College District. The contract, an interjusridictional exchange, is specifically allowed by law, and the Chancellor's Office obtained all necessary state control approvals in using this procedure. In addition we dispute your calculation that the "unnecessary costs" of using this procedure were $15,500, since the agreement paid for some the Deputy Chancellor's travel that the State would have otherwise been required to reimburse. Finally, the "unnecessary costs" you cite occurred over a period of three years--meaning that the actual additional cost each year, if any, was very small. (5)

We disagree that the Chancellor's Office created a conflict of interest by allowing the deputy chancellor to sign grants with State Center while continuing to pay him through the contract with State Center. The Vice Chancellor for Fiscal Affairs and/or the Chancellor additionally signed on all such grants to assure that there was no favoritism towards the District and to assure that each grant was appropriate. (6)

We disagree that State Center Community College District incurred "excessive" travel costs. Your report attempts to define what is excessive for a group meal paid for by a contractor by applying the standard of *individual reimbursement* rates set by the State. We know of no standard or limit imposed by law or otherwise that defines what a state agency can spend on providing a meal to a group of its employees. In the absence of such a standard, agencies should not incur unreasonable expenses for meals. We disagree that you can legally or otherwise conclude that the expense was unreasonable simply because the average cost per meal would have exceeded what an employee could have been reimbursed if he or she had paid for the meal directly. Group meals provided by hotels frequently cost more than what individuals would pay if they ordered from the hotel's restaurant menu. Group meals, however, enable meeting participants to stay together, enable some business to be conducted during the meal and enable the participants to get back to the meeting sooner than if they had all left to go eat on their own. Many times, the price for the meals is part of a negotiated package that comes along with reduced rent for conference rooms or sleeping rooms. For all these reasons we cannot agree that an average of $27 per meal, the expense you cite is clearly unreasonable or excessive.

We disagree with the Chapter headings for both Chapters 1 and 2, because we believe they are both overbroad and sensationalistic. Chapter 1 states, "The Chancellor's Office Lacks Adequate Control of the Economic Development Program." To draw this conclusion, your report would have had to investigate and analyze the entire Economic Development Program. It, in our opinion, did not. The report does document that the agency does not always comply with its own procedures in awarding grants, and that the agency does not always monitor every grant to ensure that each college complies with each requirement. But these findings do not necessarily translate into an overall finding that the Chancellor's Office lacks adequate control of the entire program. The Highway Patrol does not catch every speeder; but this doesn't mean we can conclude that the Highway Patrol lacks adequate control of highway safety. To draw this conclusion we must analyze how the Highway Patrol is applying the resources it has to deal with the issue, what the total responsibilities of the Highway Patrol are, and whether, under these circumstances, it is exerting reasonable control over highway safety. Based upon the isolated nature of your inquiry and findings, we do not believe you can conclude that the Chancellor's Office lacks adequate control of the Economic Development Program.

Chapter 2 states, "The Chancellor's Office and the Department of Education Used Fiscal Agents to Circumvent State Controls." This heading implies that these two agencies use fiscal agents as a regular practice, and that the practice of circumventing state controls is also practiced regularly. Yet, the entire chapter documents only one overall instance of allegedly inappropriate practices--the work on the Needs Assessment for the State Plan for Vocational Education. In fact, the Chancellor's Office only uses fiscal agents in rare instances; and these instances are carefully controlled to assure that they don't circumvent state controls. We have worked these

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relationships out in coordination with the Department of Finance and other ncies.

cellor's Office annually processes over 700 grants and over 60 contracts. lly the process breaks down and transactions which should be processed as are processed as grants. We are constantly monitoring and improving our s to assure that this does not happen in the future. Only rarely do contractors rmance before all required approvals are finalized. Usually, there are s which prompt these circumstances. Given the scope of your audit and the ons you have analyzed, we believe the Chapter heading "The Chancellor's nd the Department of Education Used Fiscal Agents to Circumvent State " is both overbroad and misleading. (9)

sponse to Recommendations

commendations raised in your report are taken into advisement and will be given s consideration. Again, because of the deadline for response that came during oliday season, we must reserve the right to disagree with or qualify your findings continue to verify the information and conclusions contained in the report. At this In time, however, I believe we are prepared to make the following commitments d addressing issues you have raised in the report:

1. The Chancellor's Office will comply with the revised Standing Order on tracts (Section 318) as well as the new Board Standing Order (Section 319) which ures competitive processes to award Economic Development grants. You commend that the Board of Governors reconsider its policy to exempt grants which made pursuant to an allocation formula approved by the Board. In this regard we (10) e not certain whether you are aware that there aren't any Economic Developments warded on an allocation formula basis. In addition, we are not certain you are aware t federal law requires at least some Vocational Education funds to be allocated on a mula basis. Thus, federal regulations and other ramifications may limit what the rd can actually do with respect to this recommendation.

2. The Chancellor's Office will seek additional resources to enable it to monitor nd review grant expenditures to ensure that community colleges are complying with grant requirements. In addition, the Chancellor's Office will examine whether any existing resources within the agency can be redirected to such monitoring activities without compromising performance on other mandated functions of the agency.

3. The Chancellor's Office will comply with State requirements for awarding contracts and submit complete and accurate information to the Department of General Services when requesting approval of contracts. In particular, the Chancellor's Office will ensure that it follows its own procedures by using contracts, rather than grants to award funds when it has the legal or statutory responsibility to perform the activities.

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In addition to this general response to your draft report, I'm including a number of attachments. Attachment #1 is a more detailed listing of our preliminary responses to your report. Attachment #2 sets forth the recently-adopted Standing Orders of the Board of Governors on Contracts (Section 318) and Grants (Section 319). Finally, Attachment #3 sets forth responses we received from the State Center Community College District and the Los Rios Community College District.

If you have any questions about this response or any of the attachments, please do not hesitate to contact me at 322-4005. In addition, Vice Chancellor and General Counsel, Tom Nussbaum, who coordinated the preparation of this response, is prepared to address any questions or concerns you might care to raise. Vice Chancellor Nussbaum can be reached at 445-4826.

We appreciate the opportunity to respond to your report. I would like to commend your staff for their extremely thorough review, and I look forward to working with your office and other appropriate agencies in addressing the concerns raised in the report.

Sincerely,

David Mertes

David Mertes
Chancellor

cc: Vishwas More
President, Board of Governors

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ATTACHMENT #1

PRELIMINARY RESPONSES TO AUDIT REPORT
(#94-123) DATED DECEMBER 19, 1995

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PRELIMINARY RESPONSES TO AUDIT DRAFT REPORT (#94-123) DATED DECEMBER 19, 1995

CHAPTER 1

SUMMARY

1. I recommend that the chapter title be changed to: Audit Findings: Chancellor's Office Economic Development Program 1992-93 and 1993-94. Rationale: The current title is inaccurate and misleading.

2. For the same reason, I recommend that the title of the overall report be changed to: Audit Findings for the Chancellor's Office Economic Development Program 1992-93 and 1993-94 and, Contracting Procedures Including the Department of Education.

3. Page 1-1 lines and 3 and 4 would be more accurate if they stated "did not always comply..." and if in line 11 the phrase "while the overall program match exceeded the requirement, ..." were inserted.

4. Page 1-1, paragraph 2 should be deleted. This paragraph makes inappropriate comparisons between group functions and per diem rates for State employees. District staff are not State employees and are not eligible for State rates.

5. Page 1-1, paragraph 3 should be deleted. The State's processes for contracting for an inter jurisdictional exchange process were utilized (not circumvented as stated) and as stated later in the report, the use of co-signatures was specifically to avoid any conflict of interest on the part of the Deputy in relation to State Center.

6. Page 1-2, paragraph 3, line one would be more accurate if it stated "...office did not always comply...". This entire section ignores the information provided the Chancellor's Office, dated June 27, 1995, June 30, 1995 and July 17, 1995. This included the fact that contracts with community college districts are exempt from competitive bidding by public contract and Code Sections 10340 (b)(3) and 10356 (c)(3).

7. Page 1-3, paragraph 3 ignores the information provided June 27, 1995 and fails to distinguish between the selection of a lead college which is achieved through a consensus process involving all of the colleges which that particular initiative and further draws the erroneous conclusion that selection of a "lead college" through a competitive process is more effective in identifying the "most qualified" than selection through a consensus process. There is no evidence that this assumption is true, especially in light of the fact that the entire purpose of a "lead college" is to provide leadership, coordination and technical assistance. All of these qualities are highly dependent on the ability to elicit cooperation among the colleges, not competition.

8. Pages 1-3 and 4 - We agree that staff shortages resulted in timelines not being strictly adhered to. Since the reorganization and establishment of the grants and contracts unit and attendant redistribution of workload and development of procedures, this problem has been virtually eliminated. Indeed in 1994-95 and 1995-96, all grants were fully processed, approved and mailed to the districts by July.

9. Page 1-4, paragraph 4 - We concur that more staffing is needed to provide a more thorough monitoring and review process. However, since the reorganization which established the grants and contracts unit and assigned specialists on a Regional basis this process has improved significantly as documented by the log provided December 11, 1995. Additionally, grant funds are subjected to the same scrutiny as all other funds in each district's independent annual audit.

10. Page 1-5 - We concur that technical assistance and guidelines need to be provided to create a more uniform reporting of matching funds. While the sample yielded failure to match $467,000 out of $2,898,000 data indicate that many colleges over match such that the Economic Development Program as a whole leverages an average of at least $2 to $4 for each State dollar invested. Also, copies of information provided by State Center, September 15, 1995 indicate that corrections in their matching funds were made.

11. Page 1-7 and 8 - We concur with this finding in that staff had already identified this weakness and created procedures to improve the collection and processing of quarterly and final reports as verified by the log provided December 11, 1995.

12. Page 1-8, paragraph 2 - We concur with this finding and will remind districts of the requirement for prior approval of subcontracts as well as the Board's Standing Orders (318 and 319).

13. Page 1-8, paragraph 3 through page 1-10, paragraph 3 - This entire section should be deleted in that it is inaccurate and misleading for the reasons discussed earlier in this response which include the inappropriate comparison of group functions for community college and business representatives for which there are not regulations with per diem rates for State employees. College districts do not qualify for State rates. Additionally, this section ignores the role and responsibility of State Center, under the terms and conditions of the grant, to conduct committee meetings and coordinate the statewide conference. The section is misleading in that, it implies that the travel was by State Center staff and for State Center. Both of these assumptions are inaccurate.

14. Pages 1-10 and 11 - We concur with this finding and will immediately remind the colleges of the relevant sections of the "Terms and Conditions" as well as the Board's Standing Orders. Procedures will be developed to monitor these requirements.

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15. Page 1-12 through 1-14, paragraph 1 - We concur with this finding in that staff had already identified this weakness and initiated procedures to improve this process including changes in the terms and conditions. Additionally, it should be noted that Economic Development funds are subjected to the same level of scrutiny in each district's annual independent audit as other State and federal funds.

16. Page 1-14, paragraph 2 through page 1-16, paragraph 1 - This section fails to acknowledge the differences in administration and staffing decisions at local colleges. For example, the college administers the program and staffs the program in accordance with the district's personnel policies. Many districts reassign current staff and fill behind them with temporary positions while other districts choose to use consultants or temporary personnel. We disagree with the statement that the "use of consultants conflicts with the Chancellor's Office philosophy of awarding funds to districts with the expertise to operate the programs (page 1-15, paragraph 2). This statement ignores the over all infrastructure of an organization including its Chief Business Officer and Chief Executive Officer as well as its experience, expertise and reputation with its business community and the other colleges. We believe this section should be deleted or substantially modified because its conclusions are unsubstantiated. However, we concur that it would be more appropriate to award the marketing and special project funds to State Center since that is the district overseeing the work. These funds can be redirected to State Center in 1996-97 to correct this issue. However, it should be noted that this action would not result in fewer administrative fees. The four percent indirect cost would be available to State Center. The last sentence in this section should be deleted in that it assumes that if the Chancellor's Office hired the consultants directly, it would cost less than $30,500. Given that the State Chancellor Office's operational budget is calculated at 40.1% of the personnel costs (approximately $295,547 in this case), the assumption is obviously incorrect. Additionally, the statement ignores the fact that Proposition 98 funds are local assistance funds and cannot be used by the State agency nor can they be contracted to a private entity (see Ralph Black's memo to Tone Staten dated June 30, 1995). (14) (15)

17. Page 1-16 through page 1-17, paragraph 1 - We concur with some aspects of this section and believe that as we improve the monitoring of quarterly reports, the issue will be substantially diminished. However, we disagree that expanding the scope of work of a project or extending its period of performance results in a failure to "maximize economic development grants". Indeed this may be precisely the action needed to maximize the impact of the grant. However, since this audit did not focus on the impact or performance outcomes of any grant, the heading for this section is inappropriate, insubstantial and misleading. (16)

18. Page 1-17 - We concur with this finding in that staff had identified this issue in the Fall of 1994 (see Ralph Black's memo to Tone Staten dated June 30, 1995) and has already ceased this practice.

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19. Page 1-18 - This section should be deleted in that it is both inaccurate and misleading as explained earlier in my cover letter and in the response to the over all summary report. Documents to support the appropriateness of the contract and its costs (including travel) were provided December 12, 1995. Additionally, the suggestion of a conflict of interest ignores the precaution the Agency had taken by requiring a second signature on grants awarded to State Center. Also, this statement ignores the fact that this was a continuing grant which had been originally awarded to State Center before the Deputy was employed by the Chancellor's Office. Therefore, he could not have influenced the original decision. (5) (6)

20. Pages 1-19 through 1-20, paragraph 1 - We concur with this section except for paragraph 3, page 1-19. Economic Development funds are <u>not</u> awarded by allocation. This paragraph is inaccurate and therefore, should be deleted. (10)

21. Page 1-20 - We disagree with portions of the conclusions as detailed earlier in my response.

22. Pages 1-20 through 1-21 - We concur with recommendations 1, 2, 5 and 6 and disagree with recommendations 3, 4 and 7. Recommendations three and four ignore that community colleges are independent districts with governing boards of trustees fully responsible for fiscal policies including all State and federal funds and are subject to independent audits annually. District staff are not State employees and therefore not eligible for State rates, thus such a policy would be inappropriate. Recommendation 7 is inappropriate as explained earlier. (-)

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CHAPTER 2

SUMMARY

1. Title - The title is inappropriately broad and misleading as explained in my cover letter. The only contracts reviewed were those awarded to The Resource Group, a 100% minority owned and operated small business firm in Riverside, California. Therefore, the investigation does not warrant painting the Department of Education or the Chancellor's Office with such a broad and sweeping conclusion. A more appropriate title would be: "The Chancellor's Office and the Department of Education did not appropriately or fully utilize the State's processes in awarding grants and contracts to develop the needs assessment and State Plan for Vocational Education". (16)

2. Page 2-1, paragraph 1 - The Chancellor's Office paid less than $12,000 in administrative costs and the assumption that the agency could have conducted the same level of administrative tasks at a lower cost than the approximately 4.6% paid is unsubstantiated. The Chancellor's Office reviewed and approved the products and the invoices for the assessment and the State Plan, therefore, the last sentence should be deleted and/or modified to reflect this correction. (17)

3. Page 2-1, paragraph 2 - We agree that our decision to utilize a contract and abort the original grant with Chaffey resulted in work commencing before the contract was approved. However, we believe the risk of the loss of 1/4 of a billion dollars to the State was a greater risk. We disagree that the Chancellor's Office "had no assurance that the amounts paid to the contractor were appropriate". The products and invoices were reviewed by the Chancellor's Office. (18)

4. Pages 2-3 through 2-5, paragraph 1 - The Chancellor's Office did not circumvent State contracting requirements. Both the contract with Chaffey College and the contract with The Resource Group were approved by the Department of General Services. Sole source contracting was permissible in both cases. The market survey verified that the costs were reasonable. (19)

5. Page 2-5 and 2-6 - This section should be deleted. This statement is inaccurate and misleading in that Chaffey College's employment of The Resource Group and assignment of Robert Pile as Project Director did not place Mr. Pile in any position to profit directly or indirectly from that contract. Chaffey College's Board of Trustees approved the contract and along with its Chief Business Officer approved all payments to The Resource Group. Mr. Pile's limited employment with The Resource Group in 1992 did not place him in any position to profit from the College's contract with The Resource Group in 1993. In paragraph 2, page 2-6 of the draft report, the statement referencing the Attorney General's opinion implies that Mr. Pile was an employee of the Chancellor's Office. This statement is inaccurate and thus calls into question the conclusion that Mr. Pile "<u>may</u> have violated the common law doctrine against conflicts of interest". (20)

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6. Pages 2-7 through 2-10, paragraph 1 - We concur that a number of glitches in the process occurred. Documents verifying the sequence of events were provided to the audit staff in October and again in December, 1995. The shift in the budgeted amount for the contractor with Chaffey did receive approval by the Vice Chancellor but was formally amended through General Services. The over all budget was not exceeded but the amount to Chaffey was decreased to reflect the decrease in their administrative role. We acknowledge that work on the State Plan began before the contract was fully approved by General Services. Compelling circumstances as explained in my cover letter encouraged us to take this step.

7. Page 2-11, paragraph 2 through page 2-12 - We disagree with the statement in paragraph 2 that "neither can assure that they received the services they paid for nor that the costs were reasonable". Both the products and the invoices were reviewed by the Chancellor's Office. The market survey verifies, at least under the circumstances, that the costs were reasonable. Also, it should be noted that the State Plan was a Professional Service Contract in which we paid for the product in increments (modules). There was no double billing or duplicate payment made to the contractor by Chaffey College or the Chancellor's Office. The example cited on page 2-12, paragraph three references a projected payment of $86,243 that was actually invoiced separately as $50,000 and $36,243. That is why the same services were listed in both invoices. We concur that a posting error was made by Los Rios which resulted in $5,000 being posted to the Chancellor's Office grant rather than to the contract from CDE. (18) (21)

8. Page 2-13 through page 2-15, paragraph 3 - We concur that for reasons stated earlier, work began before the contracts were fully approved. We concur that had the process been undertaken earlier, the time constraints would have been lessened. However, that is hindsight and not knowledge possessed by either the State Director or the Vice Chancellor who were new to State service and only assumed their positions in July and August of 1992. None of the staff responsible for the State Plan in 1991 and referenced in paragraph 2, page 2-15 were involved in developing the 1994-96 Plan. In fact at least four of the principle staff in 1991 had already left State service. The date on the Memorandum of Agreement (March, 1994) reflects the information acquired by this experience and an effort by the staff and the Boards to commit this information to writing and formal agreement to avoid this problem in the future. Finally, regardless of how minor the changes made by USDE, the final requirements were not available to the State until February 22, 1994. The information provided in the workshops in the fall of 1993 were utilized in developing the Plan. However, it should be noted that USDE's timeline does not accommodate the difference in the size of the task for small states like Rhode Island and a very large and diverse state like California.

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9. Page 2-15, paragraph 4 through page 2-16, paragraph 1 - The corrective action should include the corrective actions taken by the Board of Governors (Standing Order 318) as well as those taken by the Superintendent of Public Instruction. Please add that language to this section.

10. Page 2-16, paragraphs 2 and 3 - We concur with portions of the conclusions as explained earlier but disagree with the last portion of paragraph 2 and request that this portion be deleted beginning with sentence 2. The rationale for this request was provided earlier in my response (see response to Chapter2, items 5 and 7).

11. Pages 2-16 and 2-17 - We concur with the recommendations; however, we have determined that there were not overpayments to The Resource Group. This statement is inaccurate and misleading in that Chaffey College's employment of The Resource Group and assignment of Robert Pile as Project Director did not place Mr. Pile in any position to profit directly or indirectly from that contract. Chaffey College's Board of Trustees approved the contract and along with its Chief Business Officer approved all payments to The Resource Group. Mr. Pile's limited employment with The Resource Group in 1992 did not place him in any position to profit from the College's contract with The Resource Group in 1993. In paragraph 2, page 2-6 of the draft report, the statement referencing the Attorney General's opinion implies that Mr. Pile was an employee of the Chancellor's Office. This statement is inaccurate and thus calls into question the conclusion that Mr. Pile "may have violated the common law doctrine against conflicts of interest".

12. Appendix B, page 1 - The chronology of events would be more accurate if July, 1993 reflected the awarding of a grant to Chaffey College for $220,000 and October , 1993 reflected the withdrawal of that grant by the Chancellor's Office and its decision to seek DGS's approval for a sole source contract with Chaffey College as the more appropriate vehicle. Documentation of this information was provided in October and again in December of 1995. Therefore, we request that these steps be reflected on the chronology of the process to provide a more accurate picture of the sequence of events.

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ATTACHMENT # 2

RECENTLY ADOPTED STANDING ORDERS OF THE BOARD OF GOVERNORS

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(b) The Chancellor shall direct the activities and evaluate the performance of employees of the Chancellor's Office.

318. Contracts.

(a) Except as provided in subsection (b), whenever the power to contract is invested in the Board, or when, in the judgment of the Chancellor, such contracts are expressly or impliedly authorized to fulfill responsibilities or authorities vested in the Office of the Chancellor, the Chancellor is authorized in the name of the Board of Governors to enter into such contracts.

(b) The Chancellor shall secure Board approval before entering into any contract:

(1) In excess of $100,000; or

(2) Over three years in duration; or

(3) With respect to consulting services, in excess of $50,000.

The requirement for Board approval shall apply to any amendment of a contract which results in the original contract exceeding the specified limits, as well as the amendment of a contract where the amendment itself exceeds the specified limits. Under circumstances when the need to contract was not foreseeable, and when delaying approval of the contract until the next Board meeting would jeopardize the contract or frustrate its purpose, the Chancellor shall have the authority to enter into contracts in excess of the limits specified in this subsection. Before entering into such contracts, however, the Chancellor shall consult with the President of the Board.

(c) In securing the approval of contracts by the Board pursuant to subsection (b), the Chancellor shall apply the following procedures:

(1) In determining the nature, extent and need for any such contract, the Chancellor shall provide a summary of the Request for Proposal (RFP), Invitation for Bid (IFB), or other summary of the purpose and need for a contract to the Board of Governors prior to publicly releasing any such RFP or IFB, or prior to making any informal commitment to contract. The Chancellor may proceed with the release of the RFP, IFB, or other contract negotiations, unless the Board President, with or without the advice of any appropriate Board Committee designated by the President, directs the Chancellor to withhold action within a 10 day period from the date the summary is provided.

(2) In developing language for such contracts, the Chancellor shall include a provision which allows any aggrieved bidder on an RFP or IFB to protest the awarding of a contract to the Chancellor. The Chancellor shall inform the Board of any such protests, including the results of such protests. This remedy shall be in addition to the bidder's right to protest the matter to the Department of General Services.

(3) The Chancellor shall ensure that each panel of evaluators who score proposals is made up of staff from more that one division in the Chancellor's Office, including outside evaluators as appropriate, and the Chancellor shall take such other steps as necessary to ensure that evaluations and scoring are objective and fair.

(4) In requesting approval of said contracts, the Chancellor shall, at the time of distributing each regular meeting agenda to the Board of Governors, include a summary of contracts for Board approval. The summary for each contract shall indicate: the purpose of the contract; the amount of the contract; the time for performance of the contract, including whether it was advertised as a multi-year contract; the number of proposals received or whether the contract is a

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sole source contract; the number of proposals which met the minimum score for cost opening; and the party awarded the contract.

The provisions of subparagraphs (1) through (3) above shall not apply to interagency agreements with other state agencies, and other agreements necessary for the agency to receive public funds.

(d) The authorization contained in subsection (a) includes agreements, leases, contracts, and other documents, including but not limited to: service agreements, insurance agreements, fiscal, budgetary, and personnel documents, travel requests, contracts for the purchase of apparatus, furniture, equipment, supplies and books, as well as contracts entered into as necessary to receive federal funds allocated to the California Community Colleges, all within the limits of fiscal ability and sound budgetary controls and subject to such policies as may be established by the Board. (EC Section 70901(b)(5).

319. Grants.

(a) Except as provided in subsection (b), whenever the power to enter into a grant is invested in the Board, or when, in the judgment of the Chancellor, a grant is expressly or impliedly authorized to fulfill responsibilities or authorities vested in the Office of the Chancellor, the Chancellor shall have the authority to enter into such grants.

(b) The Chancellor shall secure Board approval before entering into any grant:

(1) In excess of $100,000, or

(2) Over three years in duration, or

The requirement for Board approval shall apply to any amendment of a grant which results in the original grant exceeding the specified limits, as well as the amendment of a grant where the amendment itself exceeds the specified limits. Under circumstances when the need to enter into a grant was not foreseeable, and when delaying approval of the grant until the next Board meeting would jeopardize the grant or frustrate its purpose, the Chancellor shall have the authority to enter into grants in excess of the limits specified in this subsection. Before entering into such grants, however, the Chancellor shall consult with the President of the Board.

(c) Unless specifically exempted by the Chancellor in accordance with subsection (h) of this section, all grants awarded by the Board of Governors on or after January 1, 1996, shall be awarded through competitive processes or through allocation formulas reviewed and approved by the Board of Governors.

(d) Panels evaluating or scoring grant proposals will be from more than one division in the Chancellor's Office, will include or be comprised of outside readers as appropriate, and will be comprised so as to assure objectivity and prevent conflict of interest.

(e) Grants for the performance of functions which are ongoing in nature will be awarded in cycles of between one and five years in length. In advertising a grant for an ongoing function, district personnel will be apprised of the length of the cycle, and further informed that continuance of the grant will depend on year-to-year funding, and continued satisfactory performance.

(f) A district which, prior to January 1, 1996, has been awarded a grant on a non-competitive basis for the performance of an ongoing function may continue to be awarded that grant, at the discretion of the Chancellor, for a period of up to three additional fiscal years. Retention of the grant shall depend on continued availability of funds and satisfactory performance. At the conclusion of the term, the grant for the ongoing function shall be awarded on a competitive basis.

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(g) To the extent that a grantee contracts with a private or public entity to perform certain parts of the grant, the grantee shall be required to disclose the intended purpose and amount of such subcontracting, shall agree to follow locally applicable competitive bidding processes in doing such subcontracting, and shall agree to name the subcontractors chosen.

(h) The procedures specified above shall not apply to grants which are distributed on an allocation formula basis which has been reviewed and approved by the Board of Governors. In addition, grants may be awarded competitively within regions. Finally, where there are conditions beyond the control of the Chancellor which limit competition, such as matching fund requirements or other agencies being required to select grantees, the Chancellor, in consultation with the President of the Board, shall have authority to award grants without using the competitive processes described above.

320. Claims.

The Chancellor shall execute and approve or deny all proper claims against the Board and the Office of the Chancellor.

322. Use of Name.

The Chancellor may authorize or deny, on behalf of the Board, the use of the name "California Community Colleges" in accordance with law. (EC §71025)

324. Gifts and Bequests.

The Chancellor may accept, on behalf of the Board and in the name of the State, gifts, donations, bequests, and devises in accordance with Education Code Section 71046. All gifts so accepted shall be reported to the Board. The Chancellor shall establish reasonable conditions or restrictions governing the acceptance of such gifts, donations, bequests, and devises. With respect to gifts, donations, bequests, and devises which are controversial or unusual in nature, the Chancellor may accept such items, but shall first consult with the President of the Board and such acceptance shall be submitted to the Board for ratification. (EC §71046)

326. Annuity Contracts.

Subject to Board conditions, the Chancellor may purchase annuity contracts for permanent employees of the Board in accordance with Education Code Section 71093. (EC §71093)

328. Travel Expenses.

The Chancellor may authorize the payment of actual and necessary travel expenses in accordance with Education Code Section 71040. (EC §71040)

Article 3. Consultation

330. General.

The Chancellor shall represent the Board in the system consultation process established pursuant to Education Code Section 70901. (EC §70901) In carrying out this responsibility, the Chancellor shall routinely inform the Board of the status of items in Consultation, and there will

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ATTACHMENT # 3

RESPONSE LETTERS FROM
STATE CENTER COMMUNITY COLLEGE DISTRICT
AND
LOS RIOS COMMUNITY COLLEGE DISTRICT

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State Center Community College Distric
1525 East Weldon Avenue · Fresno, California 93704
(209) 226-0720 · FAX (209) 229-7039

December 21, 1995

Dr. Ernest Leach, Deputy Chancellor
Dr. Phoebe Helm, Vice Chancellor
California Community Colleges
1107 9th Street 6th Floor
Sacramento, California 95814

Dear Doctors Leach and Helm,

ED>Net received a call today from Mr. Harvey Hunter, auditor for the California State Auditor, Bureau of State Audits. Mr. Hunter advised us that there were five areas in which State Center Community College District is named in the final audit report.

Mr. Hunter stated that in order to receive a written list of the issues we would need to contact your office. We tried to do that by telephone today but were not able to reach anyone who could assist.

According to Mr. Hunter, the Chancellor's Office will need to respond to the issues by the first week in January. Therefore, we have elected to respond to the audit issues as we understand them in hopes that this will assist you in responding to the full audit report.

AUDIT POINT #1: *FY 92/93 inadequate matching funds*

RESPONSE/COMMENTS:
On September 15, 1995, State Center was notified of discrepancy in matching funds by the audit team. A review of 92/93 showed that indeed Rio Hondo and Chaffey money had inadvertently been used for match. However, during that same review, it was also noticed that there was a substantial amount of match money that had been under-reported, or not reported at all. Additionally, Mr. Cummins, state auditor, stated they are not questioning the ISSC match.

There also seems to be a question about the formula that is being used to calculate match. Prior to 92/93 the Chancellor's office and State Center agreed to the current match formula. If there is some other formula that needs to be used we are not aware of it.

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ED>Net. through State Center. adjusted the match. The revised "match" was submitted to the auditors on October 23. 1995. via FAX and hard copy.

It is very important to note that "Match" means that all economic development money must be matched 100%. It does not mean that each individual college or grantee must match 100% even though that would be nice. So if some programs are over on match and some are under. this is acceptable because the total match for the state is being met. (13)

AUDIT POINT #2: ***Excessive travel costs***

RESPONSE/COMMENTS: As we understand this issue, the auditors state that per diem must be taken into account not only for individuals traveling on business but also for "events". For instance, if ED>Net held a conference and the attendees paid for their lunch in the registration fee we still cannot exceed the per diem for lunch. It has been presented to me by the auditors that this position applies whether the attendees are community college participants or business and industry representatives. (7)

According to district policy, conferences and meetings that include catering are paid as invoiced. The cost of food is not subject to per diem rates since those costs include hotel services, i.e. conference room usage, etc. Part of the negotiations with hotels include discounted sleeping rooms and conference space, as well as the food costs. All payments have been made within the policies of the district.

AUDIT POINT #2a: ***The District paid for hotel rooms, in conjunction with meetings, for the California Community College Deputy Chancellor and Vice Chancellor.***

This is correct. It was done one year, when notified this was an incorrect use of funds the practice was discontinued immediately. Total amount in question $1700.

AUDIT POINT #3: ***Subcontracts***

SCCCD cannot enter into sub-contracts without the Chancellor's Office written permission.

COMMENTS/RESPONSE: The auditors are referring to open purchase orders for printing, writing and computer services. These were not subcontracts and the open purchase orders were issued after reviewing bids on specific projects from several vendors. BennettFROST was a "best price" negotiated contract. We are fully aware that actual sub-contracts need the Chancellor's office approval. (24)

AUDIT POINT #4: ***Exceeding budget line items***

If a budget line is exceeded by 10% or new line items are added. written approval is needed from the project monitor. John Prentiss. Mr. Hunter cited that State Center had a total budget line item for 2 years which amounted to $ 268.680 for consultants and the

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actual expenses were $ 284,000. This encompassed the entire office staff of ED>Net, who are temporary employees or independent contractors.

COMMENTS/RESPONSE: According to COCCC policy (93/94 and currently) line items are allowed variances up to 15%. Written requests, well under the maximum 15%, were submitted to COCCC and were given verbal approval. We try to work as close to the budgeted amounts as possible but in reality the budget is a working document and, on occasion, budget items need to be transferred, increased or decreased as the year progresses and we adjust to emerging issues. The amount in question over a two year period is a 9.5% adjustment, well under the 15% once again.

AUDIT POINT #5: ***Excessive use of consultants***

The use of consultants or temporary employees, is an issue that goes beyond the normal bounds of the audit compliance. The grant agreements are one year in duration. There is no mandate in the agreement that "full time, regular employees" be utilized. There is no guarantee that any grant will become or continue to be, a "continuing" grant. The very uncertainty of this funding source makes it difficult to hire employees that a district will need to keep on the payroll well after the project is discontinued. The district must look to the best interests of all its employees when accepting a grant and must determine the best way to staff that project in a fiscally responsible manner. Therefore, this district has opted to hire temporary employees and consultants as much as possible to staff the ED>Net grant.

The State Center Community College District views the audit process as a necessary and welcomed reflection of our actual practices. It is our intention to continually revise our operations to meet all audit standards.

Your comments on our responses to the audit points would be most appreciated.

Sincerely,

Tom Crow
Vice Chancellor, External Operations

cc: Mr. Peter Krupczak, SCCCD
Ms. Jean Petty, ED>Net
Mr. Ed Eng, SCCCD
Mr. John Prentiss, COCCC
Mr. Steve Cummins, California State Auditor, Bureau of State Audits

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LOS RIOS COMMUNITY COLLEGE DISTRICT

SACRAMENTO CITY COLLEGE AMERICAN RIVER COLLEGE COSUMNES RIVER COLLEGE

December 22, 1995

David Mertes, Chancellor
California Community Colleges
1107 Ninth Street
Sacramento, CA 95814-3607

Dear Dave:

On December 20, 1995, we received a courtesy call from Harvey Hunter of the Bureau of State Audits, advising us of a draft audit report issued to your office. Mr. Hunter described those cases where findings involved the Los Rios Community College District. We would like to respond to the audit findings as appropriate, but find ourselves in a difficult situation. We are not permitted to review a draft copy of the report in order to respond to its specifics. We have spoken with your staff (with permission from the auditors) about the issues affecting Los Rios and have prepared the following response. We believe that it would be more accurate if we could review the written report, but are providing the following response to the best of our ability.

Under the heading "The Community Colleges are not providing adequate matching funds" the auditors cite two instances at Los Rios. Under grant #92-0208 the auditors indicate that Los Rios under-matched the grant by $12,722. In our proposal for this grant, Los Rios submitted a cash and in-kind budget of $137,278 which was approved in the executed agreement. The amount of State funds was somewhat greater than the district funds provided as agreed to, but the District did meet the full match obligation of $137,278. This complies with section 6 of the agreement (entitled "Match") which states: "the recipient shall provide for the contribution of a matching amount equal to the amount provided in the Agreement...". We concur that in the second case (grant #92-0250) we did not provide adequate match. (13)

Under the heading "The Community Colleges do not follow sub-contracting requirements" the auditors indicate that in one case (ASK International), the District entered into a contract without prior approval of the Chancellor's Office, and in two cases (ASK International and Catherine Ayers) entered into contracts without a competitive bid process. We concur that there is no such written documentation. The District did follow other prudent business practices but overlooked

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these written requirements. It is important to note, however, that Catherine Ayers held the position of Statewide Contract Education Specialist prior to the District's assumption of fiscal responsibility for the contract which began in 1992-93.

Under the heading "Community Colleges do not always stay within the approved grant budget", the auditors indicate that under contract #92-0250 we exceeded a budget line item by $9,990. While this observation is accurate, it should be noted that we under-expended other line items, such that the total amount charged against the grant did not exceed the total approved amount. We would agree to this finding if it were to more clearly state that reallocations of expenditures were not approved by the Chancellor's Office. There were no net over-expenditures of State funds and the heading should be retitled to reflect this.

In closing, we are extremely concerned about a process which requires us to respond to a written report which we are not allowed to see. Our response to you is virtually blind, as we have no way of being certain that we are accurately addressing the issues as written. We will rely upon your judgment in how these comments should be incorporated into your response. If there is anything else we can do to assist you please call Rob Diamond at 568-3058 or 933-2821.

Sincerely,

Queen F. Randall

Dr. Queen F. Randall
Chancellor

rd951224

cc: Tom Nussbaum (Fax 657-3844)
Dick Beymer
Louise Davatz
Rob Diamond
Debbie Travis

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Comments

Comments of the California State Auditor on the Response from the Chancellor's Office of the California Community Colleges

To provide clarity and perspective, we are commenting on the Chancellor's Office of the California Community Colleges' response to our audit report. The numbers correspond to the numbers we have placed in the response.

(1) All information in our report is complete and verified. Further, our conclusions are based on evidence provided to us by the Chancellor's Office and the community colleges, as well as the results of our tests to determine whether that evidence complied with criteria established by the Chancellor's Office.

(2) A draft copy of the report was delivered to the Chancellor's Office on December 19, 1995. According to our standard procedure of allowing agencies five working days to respond, the Chancellor's Office would have been required to respond to the report by December 26, 1995. However, because of the holiday period we extended the due date for the response to January 2, 1996. In addition, the issues presented in the audit report were discussed at various times during the course of our audit with the Chancellor's Office and again formally with management at an exit conference held on December 7, 1995. During this meeting, portions of the draft report were shared with the Chancellor's Office staff.

(3) While we agree that Economic Development grant funds are classified as local assistance funds, we believe that because the program utilizes state funds and that these funds should be reasonably spent, the Chancellor's Office could require the community colleges to comply with the State's per diem policy.

(4) The Chancellor's Office states that it had no intent to mislead the Department of General Services (DGS) when it submitted its contract to DGS for approval; however, as stated on page 31 of the report, when it submitted the contract to DGS the Chancellor's Office was fully aware that Chaffey College had already paid the contractor $168,693.

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(5) Although the Chancellor's Office disputes our calculation, its General Counsel indicated in a memo dated December 12, 1995, that the use of the interjurisdictional exchange contract resulted in excess costs of $15,000.

(6) As we state on page 22 of our report, the deputy chancellor was being paid through a contract with State Center at the time he approved the grant to State Center for fiscal year 1993-94. Therefore, we believe that the deputy chancellor should have removed himself from the process of approving any grants with State Center.

(7) We changed the text to clarify that we are not suggesting that there is a limit imposed by law for providing meals to a group of employees. However, we used the State's reimbursement rates for meals as a standard against which we can measure the cost of meals to determine whether the amounts paid were reasonable. Using this benchmark, we conclude that paying $27 for lunch when the State's reimbursement rate is $9.50 is not reasonable.

(8) We do not believe our chapter headings are overly broad. We reviewed over 41 percent of the grant funds awarded to community colleges during fiscal years' 1992-93 and 1993-94 and consistently found compelling evidence that the Chancellor's Office lacked adequate monitoring and review procedures for grant expenditures.

(9) The text has been changed to state that "The Chancellor's Office and the Department of Education Used Fiscal Agents To Circumvent State Controls To Develop the State Plan."

(10) Page 23 of our report states that Economic Development grants are *distributed* based on an allocation formula. We do not say that Economic Development grants are *awarded* on an allocation basis.

(11) Text changed.

(12) The information provided by the Chancellor's Office on these dates was not pertinent. As stated on page 6 of our report, according to the Economic Development Funding Plans which must be approved by the Board of Governors, the Chancellor's Office uses a competitive bidding process to award program grants. Therefore, whether the Public Contract Code exempts contracts with community colleges from competitive bidding is irrelevant.

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(13) The terms and conditions of the Economic Development grants require that each community college receiving a grant must provide matching funds equal to the amount of each grant they receive. Whether other colleges over-match their grants is immaterial. In addition, with regard to the information provided by State Center in September 1995, when we determined the amount of grant funds not matched, we used the most recent information as provided by the districts. The most recent information that State Center provided regarding its matching funds was dated October 23, 1995, and was included in our report.

(14) We disagree with the Chancellor's Office's contention that the use of consultants does not conflict with its philosophy of awarding funds to community colleges with the expertise to operate the program. Specifically, we question whether State Center is meeting the Chancellor's criteria for expertise when all employees paid from grant funds were either consultants or employees hired through a temporary personnel agency. Furthermore, in fiscal year 1993-94, all but one employee paid from grant funds was either a consultant or temporary employee.

(15) Text deleted.

(16) We did not conclude that extending the period of performance results in a failure to maximize economic development grants. In contrast, the examples cited in the report clearly show that some districts have excess funds that roll over from year to year. Furthermore, we stated that by allowing community colleges to retain funds for an indefinite period of time denies other community colleges the opportunity to receive grant funds.

(17) The Chancellor's Office paid $12,000 to two fiscal agents who issued five payments to the contractor. We do not believe that the State's process to issue five warrants would cost $2,400 per warrant.

(18) We found no evidence that the invoices were ever received by the Chancellor's Office. The invoices were submitted directly to the fiscal agent who simply paid the contractor and was not involved in monitoring the progress of the work.

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(19) The Chancellor's Office contention that they did not circumvent state contracting requirements is incorrect. As stated on page 27 of our report, the Chancellor's Office used fiscal agents to obtain the services of a specific contractor. We also state that by using fiscal agents, departments can specify the use of funds without subjecting them to state review or oversight. Furthermore, as stated on page 30 of our report, the

Chancellor's Office submitted erroneous and misleading information to DGS justifying a sole-source contract after the work was nearly complete.

(20) We do not imply that Mr. Pile was an employee of the Chancellor's Office. In fact, on page 29 we clearly state that Mr. Pile is an employee of Chaffey College. In addition, the common law doctrine applies to public officials; therefore, it is applicable to this case.

(21) Because we found inadequate controls over payments and that several invoices submitted to the fiscal agents contained charges for the same service, the Chancellor's Office cannot assure that the payments were reasonable or appropriate. As stated on page 40 of our report, our recommendation is simply that the Chancellor's Office should review the payments made to the contractor to determine whether the amount paid were appropriate and, if necessary, recover any overpayments.

(22) The corrective action taken by the Chancellor's Office is presented in Chapter 1.

(23) The Chancellor's Office was unable to provide us with evidence that they attempted to award a grant to Chaffey College. However, the contract awarded to Chaffey College was approved on February 23, 1994.

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California State Auditor's Comments on the Responses by State Center and Los Rios Community College Districts

(24) The instances referred to in our report are subcontracts with consultants, not the open purchase orders State Center discusses.

(25) The terms and conditions of the Economic Development grants state that changes in budget line-item amounts up to and including 15 percent of the total budget amount require prior **written, not verbal,** approval of the Chancellor's Office. Any changes in excess of 15 percent require a formal amendment to the grant.

(26) The district is incorrect that they did not have an opportunity to respond to the audit report. While conducting fieldwork at the Los Rios Community College District (district), we met with officials at the district to discuss audit issues as they developed. In addition, on October 18, 1995, we held a formal exit conference with the Chancellor, Assistant Chancellor of Business Affairs, and other management staff at the district. At this exit conference, we distributed an outline that summarized the issues and we discussed each of the audit issues in detail. Finally, in December 1995, we discussed issues with district staff via telephone to ensure that they understood the context in which matters concerning the district were included in the audit report.

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DELAINE EASTIN
State Superintendent of Public Instruction

January 2, 1996

Kurt R. Sjoberg
California State Auditor
660 J Street, Suite 300
Sacramento, CA 95814

Dear Mr. Sjoberg:

Thank you for the opportunity to review and comment on your draft audit report titled, "California Community Colleges: The Chancellor's Office Inadequately Controlled Its Economic Development Program and, Along with the Department of Education, Circumvented State Contracting Procedures." In general, the California Department of Education (CDE) supports your recommendations for ensuring compliance with state contracting procedures. As stated in your audit report, when State Superintendent of Public Instruction, Delaine Eastin, assumed office in January of 1995, she strengthened CDE procedures for approval and use of contracts. Thus, the CDE has already taken steps to assure future procedural compliance.

The CDE, however, respectfully disagrees with your final audit recommendation which requests that the CDE "[d]etermine whether the amounts paid to The Resource Group for the needs assessment and the state plan were appropriate and, if necessary, recover any overpayments." There is no indication from any finding in your audit report that the needs assessment and the Carl Perkins Vocational and Applied Technology Education Act State Plan (State Plan) were in any way deficient. The CDE feels that it did receive the services it paid for and -- more importantly -- the U.S. Department of Education (USDE) unconditionally approved the State Plan. Before even more resources are expended, at least some proof of "inappropriateness" should be required. (1)

The CDE appreciates your acknowledgment in the audit report "that the preparation of a state plan is a complex project that requires a large investment of time and resources" and would like to reiterate the conditions, pressures and environment in which the State Plan and needs assessment were developed in 1993-94. In 1991, the USDE had significant concerns about the quality of the State Plan submitted by the

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The California State Auditor's comments on this response begin on page 89.

State of California. As a result, USDE delayed funding to California, the federal vocational education grant was awarded to California on a conditional status basis, and the funding to California was allocated in installments. Thus, there existed tremendous pressure on the State of California to develop a State Plan for 1994-96 that was a quality, comprehensive document - accurate, complete, timely and in the proper format.

The CDE and the Office of the Chancellor of the California Community Colleges (Chancellor's Office) joined for the first time as co-equal partners to design, fund, and oversee the statewide vocational needs assessment upon which the 1994-96 State Plan would be based. In a proactive effort to address concerns of the State Council on Vocational Education (SCOVE) over the lack of participation by service providers and practitioners in the development of the 1991 State Plan, the CDE and the Chancellor's Office embarked on a broadly collaborative, statewide development process. The development of the State Plan for 1994-96 involved over 1,700 individuals in the needs assessment, 100 educational leaders in formal committee meetings to analyze the needs assessment, 300 field personnel and 50 statewide agencies to develop conclusions and recommendations from the needs assessment data, 1,200 reviewers of the draft State Plan, and 5 regional public hearings on the contents of the State Plan.

The uniqueness of this statewide coordination effort was exceptional. Unfortunately, the CDE and Chancellor's Office found they had little time to complete the project by the May 1, 1994 State Plan due date. The CDE and the Chancellor's Office required the use of professional services with the expertise to complete the projects on time in order to guarantee an allocation of nearly $250 million in Carl Perkins Vocational and Applied Technology Education Act funds for the State of California. The CDE and Chancellor's Office met with SCOVE staff to discuss the scope of work, the qualifications needed to complete the projects, and the resources available. SCOVE strongly expressed the need for obtaining the services of an independent third party to complete the needs assessment.

The Resource Group is one of the state's largest holders of proprietary business, occupational, and labor market data. In 1993 the Resource Group had developed a sampling of 10,000 businesses throughout California that had indicated their current and future workforce needs as well as the skill requirements for each of the positions they now employed - proprietary data which could be used to develop the needs assessment for California, on which the State Plan would be based. The Resource Group had the expertise and resources needed by the CDE and the Chancellor's Office.

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With the assistance of The Resource Group, the CDE and Chancellor's Office produced a State Plan which exemplified intersegmental collaboration and coordination with local practitioners and service providers. The State Plan was delivered to USDE on time and received commendation from USDE officials for its quality. The State of California received unconditional approval to spend the Carl Perkins Vocational and Applied Technology Education funds effective July 1, 1994. Thus, in a very real way the CDE and Chancellor's Office received the final product for which they paid.

It is in this context that the findings in Chapter 2 of your draft audit report must be reviewed. The CDE had to produce the State Plan by May 1, 1994. The CDE did its best to comply with state contracting procedures and at the same time produce a quality State Plan for California. The CDE's comments on specific portions of the draft audit report follow.

The CDE used the most qualified contractor and paid a reasonable amount for the needs assessment and State Plan.

In Chapter 2, the draft audit report concludes in the first section that "by using fiscal agents to pay The Resource Group" and "circumventing the competitive bidding process," the CDE "cannot assure that it used the most qualified contractor" and cannot assure "that the amount paid to the contractor was reasonable." As mentioned above in reference to the exceptional qualifications required to provide services for the CDE and Chancellor's Office, The Resource Group held valuable proprietary information for the needs assessment. In addition, the Resource Group had the expertise and resources for compiling the data needed to complete the State Plan. Contrary to statements made by the auditors, The Resource Group was selected after extensive consultation with SCOVE and was the most qualified contractor known to California vocational education practitioners and experts. (2)

The audit report states that the CDE cannot "assure that [it] received the services they paid for" and "that the costs [it] paid for the services were reasonable." The CDE fully understands the amount of work and resources it took to complete a quality State Plan. The CDE worked closely with the Chancellor's Office and The Resource Group throughout the completion of the needs assessment and development of the State Plan. During the conduct of both projects, the CDE received draft copies of work products for review. The CDE and USDE were pleased with the final State Plan. Although the work product has passed the final evaluative litmus test -- approval by USDE -- the auditors nevertheless appear to be making a contrary judgment on the quality of services received when the draft audit report recommends a new evaluative review and even implies overpayment.. The CDE feels that it did receive the services it paid for and, absent some substantial tangible (1)

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evidence to the contrary, believes a new review at this time would be a cost ineffective expenditure of its resources.

The CDE has no authority or control over local conflict of interest matters.

In the second section of Chapter 2 of the audit report the auditors imply that in some way the CDE created a conflict of interest for the superintendent of East San Gabriel Valley Regional Occupation Program (East San Gabriel). The CDE has responsibility for ensuring that its own employees follow all conflict of interest requirements, including appropriate action if conflict of interest requirements are violated. The CDE has no responsibility for the conflict of interest of East San Gabriel employees; the enforcement of East San Gabriel conflict of interest requirements is a responsibility of East San Gabriel.

Whether or not a conflict of interest occurs depends on the circumstances involving a particular public official. The individual is responsible for making sure that he or she avoids conflicts. Although it would be unfortunate if the CDE were to suggest a course of action that would result in an individual conflict of interest, the individual official is nevertheless responsible for avoiding his or her own conflicts.

The auditors appear to have discovered serious questions about the propriety of the East San Gabriel superintendent's activities. Because these conclusions involve potential Government Code section 1090 and section 87100 violations, we believe your office should contact the governing board of East San Gabriel as well as the Fair Political Practices Commission. The CDE has no jurisdiction over conflicts of interest by local officials. The CDE will transmit the final audit report to East San Gabriel.

The CDE withdrew its request for approval of a contract amendment.

The fourth section of Chapter 2 of the audit report discusses a contract amendment which the CDE submitted to the Department of General Services (DGS) for approval and subsequently withdrew before the amendment was approved by DGS. The contract amendment submitted to DGS did not contain false statements. The contract amendment stated that the "contractor is developing and completing an assessment to determine the quality of vocational education programs in California. This amendment adds funding for a comprehensive set of activities and deliverables required to generate and transmit the 1994-96 . . . State Plan." The CDE made no purposeful statements in the contract amendment to indicate that the contract work had not begun or was planned to begin in the future.

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The CDE had control over project products.

In addition, the fifth section of Chapter 2 of the report indicates that the CDE "lacked control over project payments" and therefore, cannot "assure that [it] received the services [it] paid for, nor that the costs [it] paid for the services were reasonable." As stated above, the CDE worked closely with the Chancellor's Office and The Resource Group during the needs assessment and State Plan projects, reviewing draft copies of work products and communicating product needs. The CDE closely monitored both projects to ensure timely completion, USDE unconditionally approved the State Plan, and the CDE feels that it received the services paid for and that costs were reasonable.

The auditor's statement of "lack of control" is documented by the information in Table 4 which indicates that the CDE paid The Resource Group $25,000 more than the budgeted cost for development of the State Plan. The CDE paid $25,000 over the budgeted amount to The Resource Group to cover the cost of producing 1,200 additional copies of the State Plan for distribution to local educational agencies in California. The CDE feels that this was an appropriate charge for the additional copies of the State Plan. Enclosure 1 contains a description of the services and costs which comprise the $25,000 charge. (4)

If you have questions about the CDE's response to your draft audit report, please contact the CDE's Audit Response Coordinator, Peggy Peters, at (916) 657-4440.

Sincerely,

Ruth A. McKenna
Chief Deputy Superintendent for
Instructional Services

Enclosure

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December 14, 1995

To: Susan Reese

Fr: Esteban Soriano

Re: Basis of $25,000.

Susan, I'm sorry that a hectic sechedule has prevented us from talking by telephone. I understand that you have asked the basis for the $25,000 invoice or how costs added to $25,000. Here is what our records reflect. Of the nearly 1,500 plans produced, some 1,200 were specifically for CDE's use (field folks, districts, ROP's, etc.). The balance were shared for joint use stuff.

Here is what our costs were based on the 1,200:

# pages copied = 522,000 @ $0.05/ea=	$ 26,100
1200 sets of covers @ $1.50 ea=	1,800
1200 2" comb spines/punched @ $2.25 es=	2,700
1/2hr per for assembly/handling @ $19.50/hr=	11,700
Mailing most and shipping balance to CDE @ 4.20 ea=	5,040
Actual Costs for this special CDE activity:	$ 47,340
Our actual billing to CDE:	$25,000

The actual amount does not include colored paper, two-sided copying of the intro sections to each section, the 1200 envelopes, the preparation of the 1,200 mailing address forms, the renting of the pickup to haul things back and forth from the assembly area to the office and then to the post office and then the balance to the airport, supervision costs, the combined 45 hours of page by page review for quality control, etc. This, if detailed out, would be about $4,000 more, or a grand total of about $51,000 for this task. In the end, we billed $25,000.

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Comments

Comments of the California State Auditor on the Response from the Department of Education

To provide clarity and perspective, we are commenting on the Department of Education's response to our audit report. The numbers correspond to the numbers we have placed in the response.

(1) Because it did not review all the invoices that its fiscal agents paid for both the needs assessment and the state plan, we believe that the department cannot assure that the amounts paid to the contractor were appropriate. Therefore, we recommend that the department simply review the invoices to assure that the amounts paid to the contractor were appropriate.

(2) The department did not provide us any evidence that it used any type of reasonable process to determine that The Resource Group was the most qualified contractor for preparing both the needs assessment and the state plan.

(3) As noted on page 30 of the report, the superintendent of East San Gabriel informed the department that in December 1993, she had worked for The Resource Group drafting a portion of the state plan. Therefore, the department was aware that the superintendent had a potential conflict of interest when it asked her to accept a grant and use the funds to pay The Resource Group.

(4) We believe that the example cited by the department further supports our conclusion that it cannot assure that the payments made to the contractor by the fiscal grants were appropriate or reasonable. In its response the department stated that the $25,000 that it paid over the budgeted amount for the state plan is appropriate; however, we noted that the department requested support for this expenditure from the contractor after we brought it to the department's attention. Furthermore, the memorandum the contractor sent to the department showing the basis for the additional $25,000 is dated December 14, 1995, 18 months after the payment was made.

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cc: Members of the Legislature
Office of the Lieutenant Governor
Attorney General
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps

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